



Report on the Evaluation of National Defense PP&E Reporting Approaches

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Table of Contents

	<u>Page</u>
Executive Summary	i
Section I Introduction.....	1
Background	1
Objectives and Methodology	1
Report Sections	2
Section II Summary of the ND PP&E Acquisition Process.....	4
Section III Summary of Financial Reporting Objectives.....	9
Introduction.....	9
Reporting Objectives Relevant to ND PP&E	10
User Needs	13
Section IV Financial Reporting Approaches, Recommendation, and Basis for Conclusion	15
Introduction.....	15
Description of the Reporting Approaches.....	15
Comparison of Approaches with Financial Reporting Objectives	16
Comparison of Approaches with User Needs	22
Conclusion	22
Recommended Approach and Basis for Conclusion	23
Section V Summary of the DoD's Accountability and Accounting Systems	26
Introduction.....	26
Accountability Systems	26
Accounting Systems.....	28
Section VI Audit Issues	31
Introduction.....	31
Audit Issues.....	33
Section VII Implementation Issues, Cost Estimates, and Timelines	36
Introduction.....	36
Policies and Procedures	37
Systems Changes	37
Training	40
Summary.....	40

Table of Contents

Page

APPENDICES

Appendix A – Recommended Definition and Standard.....A-1

Appendix B – Financial Reporting Objectives.....B-1

Appendix C – Discussion of User CommentsC-1

Appendix D – DoD’s Accountability and Accounting SystemsD-1

Appendix E – Components of Full CostE-1

Appendix F – AcronymsF-1

Executive Summary

Background

The Federal Accounting Standards Advisory Board (FASAB) began deliberations on the accounting for, and reporting of, weapons systems in the mid 1990's. In 1995, the FASAB issued a standard that referred to weapons systems as Federal Mission Property, Plant, and Equipment (PP&E), as part of a broad standard on accounting for PP&E. Since then, the FASAB has issued standards that prescribed financial reporting requirements for weapons systems and modified the definition of Federal Mission PP&E to National Defense PP&E (ND PP&E). Most recently, the FASAB issued an exposure draft of a proposed standard to modify ND PP&E accounting and reporting requirements. FASAB deliberations on the proposed standard highlighted the differences of opinion on this subject.

To assist the FASAB in its deliberations, the Department of Defense (DoD) engaged KPMG LLP (KPMG) to: (1) develop a tutorial for the FASAB to assist it in understanding the complexity of the DoD ND PP&E acquisition process, (2) evaluate various ND PP&E accounting and reporting approaches and, (3) recommend an approach that will provide users of DoD financial statements with meaningful and analytically useful ND PP&E information that can be implemented reasonably by the DoD. KPMG provided the tutorial to the FASAB in June 2000. This report includes KPMG's evaluation of various accounting and reporting approaches and our recommendation for further FASAB consideration. The report also includes a discussion of related implementation and audit issues.

Evaluation Methodology

KPMG relied on three primary sources of information in completing its evaluation. First, we obtained an understanding of the ND PP&E acquisition process, not only to provide the required tutorial to FASAB, but also to obtain an understanding of the DoD procurement process, acquisition systems, and existing DoD methods of, and systems used in support of, accounting for ND PP&E. Second, KPMG analyzed the objectives of financial reporting issued by the FASAB and other standard setting organizations to assess the usefulness of each approach in satisfying the objectives. Third, we surveyed users of ND PP&E financial information and other interested parties to determine the relevance of the approaches to their informational needs. We also reviewed the DoD's policies, accountability and accounting systems capabilities, and other information to evaluate its ability to implement each approach.

Acquisition process. KPMG's acquisition tutorial described the life cycle and complexities of the ND PP&E acquisition process. The ND PP&E acquisition program life cycle, which can last for decades, begins with conceptualization and design, follows with research, development, test, and evaluation, and production, and concludes with procurement, modification and, finally disposal.

The costs of an acquisition program include the costs associated with each phase of the acquisition life cycle, except for the cost of disposal. Tracking these costs is an extremely complex process involving numerous appropriations, contracts, and hundreds--if not

thousands--of contract line items and thousands of associated disbursement and accounting transactions.

DoD's ND PP&E financial reporting to Congress and others is on current acquisition programs and is tied to the budget process. Congress formally monitors Major Acquisition Programs through reports prescribed by statute, and the DoD monitors other acquisition programs internally in a similar manner.

Objectives of financial reporting. Standards setting organizations, including the FASAB, issue concepts statements, which include financial reporting objectives, to guide their standards setting efforts. Given the importance of objectives to the standards setting process, KPMG analyzed the objectives of federal financial reporting issued by the FASAB to provide a basis for its evaluation of the various accounting and reporting approaches.

The objectives are to provide information that will assist users in assessing:

Budgetary Integrity – how budgetary resources have been obtained and used and whether their use was in accordance with legal authorization, the status of budgetary resources, and how budgetary information relates to the costs of programs.

Operating Performance – the service efforts, costs, and accomplishments of an entity, the manner in which these efforts and accomplishments have been financed, and the management of the entity's assets.

Stewardship – the impact on the country of the government's operations and investments for the period and how, as a result, the government's and the nation's financial condition have changed and may change in the future.

Systems and Controls – whether financial management systems and internal accounting and administrative controls are adequate to ensure that transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purpose authorized, and recorded in accordance with federal accounting standards.

User Surveys. Given that the objectives of financial reporting are to satisfy user needs, KPMG surveyed 14 individuals representing potential users from inside the DoD, other government organizations, and the private sector. Those surveyed included representatives of non-federal organizations, Congressional staff and Legislative Branch representatives, a non-DoD federal executive, and DoD program managers.

The survey focused on the decision usefulness of various reporting approaches and on the relevance of other information, such as depreciation of ND PP&E, condition reporting, the reporting of planned costs for ND PP&E acquisition programs, principally Major Acquisition Programs, and on the importance of audited ND PP&E information.

Policy and System Reviews. KPMG reviewed the DoD's policy documents and system functional capabilities. The objectives of these reviews were to evaluate whether existing policies included sufficient guidance for the effective implementation of the approaches

discussed herein, including KPMG's recommended approach, and whether systems had the functional capabilities to capture the required information.

Evaluation Results

KPMG evaluated four ND PP&E accounting and reporting approaches: (1) capitalizing and reporting ND PP&E on the balance sheet, (2) capitalizing and reporting ND PP&E as Required Supplementary Stewardship Information (RSSI), (3) reporting units of ND PP&E as RSSI, and (4) reporting ND PP&E investments as RSSI.

Capitalizing and Reporting ND PP&E on the Balance Sheet

Capitalization involves the accounting for, and reporting of, costs that provide a future economic benefit or have future service potential. In traditional accounting, these costs are expensed over the benefiting periods. In budgetary accounting, these costs are expensed when incurred.

This approach provides information or a basis for measuring operating performance and assessing stewardship. However, it does not facilitate assessing budgetary integrity.

A slight majority of users surveyed favored this approach. The reasons varied from the belief that ND PP&E represents an economic resource with future service potential to ND PP&E information being necessary to demonstrate accountability. Those not favoring this approach expressed the view that ND PP&E investments are "sunk costs", and the associated information would not be used as a basis for future decisions.

Capitalizing and Reporting ND PP&E as RSSI

RSSI is a reporting category unique to the federal government. RSSI is the vehicle for reporting information about the cost of federal resources that are not defined as assets, and, accordingly, are not included as such in the financial statements, but are important to an understanding of the financial condition of the federal government in that they provide a future economic benefit or have future service potential. The amount reported as RSSI under this approach is the same as the amount reported under the capitalization on the balance sheet approach. However, under this reporting approach, ND PP&E program acquisition costs are accounted for and reported in the financial statements as expenses when incurred, a budgetary focus.

This approach provides information for assessing stewardship. However, it impedes the DoD's ability to measure operating performance since it includes the annual costs of ND PP&E acquisition programs in operations, overstating the annual cost of operations.

The users surveyed expressed the same views about this approach as they did about the balance sheet approach.

Reporting Units of ND PP&E as RSSI

Reporting units as RSSI involves reporting physical quantities of ND PP&E that provide a future economic benefit or have future service potential. Under this approach, the costs of ND PP&E acquisition programs are expensed when incurred.

Unit reporting does not provide a basis for assessing budgetary integrity, operating performance, or stewardship. Monetary information is needed to make these assessments. Moreover, accounting concepts and standards have few references to the reporting of quantity information alone. The principal reference is in discussions of service efforts and accomplishments, principally in terms of program outputs.

A strong majority of the users surveyed expressed the opinion that unit information was useful in demonstrating accountability and, when coupled with condition assessment information, provides a limited¹ basis for assessing military readiness.

Reporting ND PP&E Investments as RSSI

Reporting ND PP&E investments as RSSI involves reporting of current year and cumulative expenses associated with ND PP&E acquisition programs. This approach would also provide information on the cumulative expenses of ND PP&E acquisition programs. The total of the cumulative information would be similar to that capitalized under the balance sheet and RSSI approaches. Under this approach, the costs of ND PP&E acquisition programs are expensed when incurred.

This approach principally provides information for assessing budgetary integrity. It would provide information for comparison with ND PP&E acquisition program budgets. However, as with other RSSI reporting approaches, it impedes the DoD's ability to measure operating performance since it overstates the annual cost of operations by expensing the annual costs of ND PP&E acquisition programs.

Some users expressed a preference for this information. The prevalent view was that this information would be useful in determining whether actual ND PP&E program acquisition costs were deviating significantly from budgeted costs. Others expressed the view that this information would assist in assessing whether the Military Departments received value for costs incurred, albeit it is unclear how this information alone would assist in that determination.

Depreciation and Condition Accounting and Reporting

KPMG expanded its evaluation to include depreciation and condition accounting and reporting due to the implications of certain approaches. Both depreciation and condition accounting and reporting are relevant to assessing operating performance and stewardship. Based on our overall evaluation, KPMG believes that depreciation is not an appropriate measure of period costs for certain categories of ND PP&E given the extensive maintenance involved in keeping such PP&E in a combat ready state. In view of the importance of readiness, KPMG believes that condition

¹ *Military readiness is assessed by more than the condition of military equipment. Readiness also includes the availability of equipment and the availability of trained military personnel.*

reporting, which provides limited information about readiness, is essential to an assessment of operating performance and stewardship.

Conclusion

KPMG concluded that none of the foregoing approaches alone satisfies all of the financial reporting objectives or the operational needs of the DoD. Consequently, we developed an alternative approach that includes several informational components for consideration by the FASAB. We discuss this alternative approach below. Appendix A - *Recommended Definition and Standard*, includes a detailed recommended revision of the ND PP&E definition and standard.

Recommended ND PP&E Accounting and Reporting Approach

KPMG believes that the definition of, and the standard on, accounting for, and reporting of, ND PP&E should be designed to provide optimal information for achieving the objectives of federal financial reporting. It should also satisfy the information needs of financial statement users and, to the extent possible, replicate the manner in which the DoD acquires, classifies, and accounts for ND PP&E. We believe the recommended approach discussed below will achieve the objectives, satisfy the needs of users, and assist the DoD in improving the quality of information used to manage ND PP&E acquisition programs.

To this end, KPMG recommends that the definition of ND PP&E be modified to more closely reflect the operating environment of the DoD and to facilitate compliance with the recommended standard. This includes a recommendation to reclassify certain PP&E currently defined as ND PP&E by SFFAS No. 11 to appropriate non-ND PP&E categories. Examples include Weapons Systems Support Principal End Items, Weapons Systems Support Real Property, and missiles other than Intercontinental Ballistic Missiles and Submarine Launched Ballistic Missiles.

KPMG recommends that the standard on accounting for, and reporting of, ND PP&E provide for the capitalization on the balance sheet of ND PP&E acquisition programs. The conceptual basis for this recommendation is that ND PP&E represents an economic resource with future service potential. KPMG also considered capitalization of the cost of individual items of ND PP&E. However, this approach would add a level of accounting on top of the current process that the DoD uses to manage, account for, and report on ND PP&E, which is by acquisition program. KPMG does not believe the costs associated with the extraordinary changes to systems and processes required by such an approach could be justified from a cost/benefit perspective.

With respect to the periodic measurement of cost and operating performance, given that Major End Item (defined in Appendix A - *Recommended Definition and Standard*) ND PP&E are maintained in a ready state through a continual maintenance and repair regimen, the cost of which is currently captured as part of the cost of operations, and because such items have an unpredictable useful life or are susceptible to premature obsolescence, KPMG does not recommend depreciation accounting and reporting for these items. Other ND PP&E would be subject to depreciation because the associated ND PP&E generally has a more predictable life and is less susceptible to premature obsolescence. KPMG recommends that the FASAB acknowledge the propriety of composite depreciation techniques as an acceptable approach.

The standard also should include a requirement to disclose the quantity and condition of ND PP&E Major End Items to provide information useful in assessing the effectiveness of the DoD's management of such items.

To address budgetary integrity, the standard should provide for disclosure of current year and cumulative cost information along with planned cost and unit output information for a limited number of major ND PP&E acquisition programs. This proposed requirement would provide readers with information on a defined number of individual major ND PP&E acquisition programs for comparison with relevant internal planning and budgetary data.

Finally, the FASAB should give careful consideration to two important issues, capitalization of existing ND PP&E and effective dates for implementing the standard. We have recommended ways to address these issues.

Implementation and Audit Issues

The DoD asked KPMG to identify implementation and audit issues associated with the foregoing approaches and the approach recommended by KPMG, in the event the recommended approach differed from the approaches discussed above.

KPMG identified four broad issue areas that affect the DoD's ability to produce accurate ND PP&E information and in turn the auditor's ability to obtain and evaluate evidential matter relating to ND PP&E. The issue areas pertain to the adequacy of accounting policies, information systems, documentation in support of ND PP&E, and internal controls.

The DoD must successfully address these areas in order to ensure the accuracy of ND PP&E information and enable the auditor to form an opinion on the financial statements of the DoD and Military Departments. With regard to documentation in support of the valuation of ND PP&E at transition to the proposed standard, KPMG recommends that the FASAB adopt a standard that minimizes the costs of valuation.

Conclusion

The report that follows demonstrates that a single financial reporting perspective does not satisfy the objectives of federal financial reporting. It examines the objectives of federal financial reporting and the views of a limited group of users of ND PP&E financial information and others with an expressed interest in federal financial management to arrive at a recommended approach that more fully addresses the objectives than does the current standard. The recommendation is accompanied by a detailed standard for consideration by the FASAB.

The report also includes a discussion of implementation issues and actions that the DoD should take to effectively implement the recommended standard and associated costs. To provide a corporate perspective, KPMG recommends that the DoD establish a cross-functional management approach for implementing the recommended standard because implementing such a standard will require the cooperation and efforts of the DoD acquisition, procurement, logistics, and financial management communities within the Offices of the Secretary of Defense, the Military Departments and Defense Agencies.

Section I - Introduction

Background

The Federal Accounting Standards Advisory Board (FASAB) has studied accounting and reporting approaches for National Defense Property, Plant, and Equipment (ND PP&E) for a number of years. In 1995 the FASAB issued Statement of Federal Financial Accounting Standards (SFFAS) Number 6, *Accounting for Property, Plant, and Equipment*, which addressed the accounting for, and reporting of, Federal Mission Property. This standard provides for expensing the costs of Federal Mission Property when incurred.

In 1996, the FASAB issued SFFAS Number 8, *Supplementary Stewardship Reporting*, which required reporting, among other things, the cost of Federal Mission Property in the form of required supplementary stewardship information. Supplementary stewardship reporting is designed to report on the federal government's stewardship over resources that are not defined as assets and, accordingly, are not included in financial statements.

In 1998, the FASAB issued SFFAS Number 11, *Amendments to Accounting for Property, Plant, and Equipment – Definitional Changes*, which amended SFFAS Numbers 6 and 8. SFFAS Number 11 replaced the term Federal Mission Property with National Defense Property, Plant, and Equipment (ND PP&E).

In the late 1990's, the FASAB also issued an exposure draft to amend SFFAS Number 6. The exposure draft included a proposal to replace the requirement to account for, and report, cost information in the supplementary stewardship report with a requirement to report ND PP&E unit and condition information. The FASAB held a public hearing on these proposals. Because of the divergent views on the accounting for, and reporting of, ND PP&E, the FASAB has been unable to reach a final conclusion on revisions to the current standards.

Because of the significance of ND PP&E and the desire for a standard that addresses the needs of users of ND PP&E information, the Department of Defense (DoD) engaged KPMG to: (1) develop a tutorial for FASAB describing the ND PP&E acquisition process and (2) evaluate alternative accounting and reporting approaches for ND PP&E, including approaches that have not been considered by the FASAB. KPMG presented the tutorial on June 9, 2000. This is KPMG's report on its evaluation of ND PP&E accounting and reporting approaches.

Objectives and Methodology

Objectives

The objectives of this engagement were to evaluate various approaches to account for, and report ND PP&E and to recommend a standard that will provide users of DoD financial statements with ND PP&E information that is meaningful, has analytical utility, and can be implemented reasonably by the DoD.

To achieve these objectives, KPMG designed an approach that consisted of:

1. Defining the relevant objectives of federal financial reporting based on the objectives of: (1) federal financial reporting as contained in the FASAB's Statement of Federal Financial Accounting Concepts Statement Number 1, (2) financial reporting for business enterprises and nonbusiness organizations included in concepts statements issued by the Financial Accounting Standards Board (FASB), and (3) financial reporting for state and local governments included in the concepts statement issued by the Governmental Accounting Standards Board (GASB).
2. Ascertaining the needs of users of ND PP&E information and other parties with a stated interest in reporting of ND PP&E information.
3. Identifying the standards explored by the FASAB for reporting ND PP&E, including the current standard.
4. Assessing the relevance of the current standard and the standards explored by the FASAB for meeting the objectives of federal financial reporting and other relevant objectives contained in FASB and GASB concepts statements.
5. Considering ND PP&E reporting approaches to effectively meet objectives of federal financial reporting and the relevant FASB and GASB objectives and the needs of users of ND PP&E information.
6. Understanding and assessing the sufficiency of the DoD ND PP&E accounting and reporting infrastructure for complying with accounting and reporting approaches that would effectively meet the objectives and needs in 5 above.

In addition, KPMG reviewed the Chief Financial Officers Act of 1990 (CFOs Act) to obtain an understanding of the purpose of the legislation that led to the creation of the various aspects of the federal financial management improvement effort, including the current federal accounting standards setting structure. The stated purpose of the CFOs Act relevant to this evaluation is the production of complete, reliable, timely, and consistent financial information for use by the Executive Branch of the Government and Congress in financing, managing, and evaluating federal programs.

The foregoing objectives of the CFOs Act were a critical component of this evaluation. They focus on the needs of management of the federal government as opposed to external parties, which is the focus of reporting standards issued by non-federal standards setters, with the possible exception of GASB.

Report Sections

This report contains the following additional sections:

Summary of the ND PP&E Acquisition Process. Section II is a summary of the ND PP&E acquisition process, as presented in KPMG's Defense Acquisition Management System Tutorial

dated June 9, 2000. The purpose of this summary is to facilitate an understanding of the complexity of the ND PP&E acquisition process and to assist the FASAB, the DoD managers, and others in understanding how that process affects ND PP&E accounting and reporting.

Summary of Financial Reporting Objectives. Section III is a summary discussion of the objectives of financial reporting. It also includes a summary of the results of KPMG's user surveys. Standards setting organizations issue concepts statements that include objectives to guide them in the development of standards useful for various parties, including management. An understanding of these objectives and their relevance to the various ND PP&E accounting and reporting approaches discussed in this report is important to gain an understanding of the reasoning for the final recommended ND PP&E accounting and reporting standard. The concepts statements provide that financial reports should include information useful to managers and other users. Given the importance of user needs in the establishment of meaningful financial reporting standards, KPMG interviewed individuals from non-federal organizations, congressional staff and Legislative branch agency representatives, a representative of a non-DoD Executive Branch agency, and the DoD program and finance managers.

Financial Reporting Approaches, Recommendation, and Basis for Conclusion. Section IV includes KPMG's recommendation on accounting for, and reporting of, ND PP&E in the DoD's annual financial statements. It is based on an understanding of the ND PP&E acquisition process, an analysis of the objectives of financial reporting, and input from users. KPMG's recommendation is accompanied by a revised definition of ND PP&E, as well as a revised ND PP&E accounting and reporting standard, which are presented in Appendix A - *Recommended Definition and Standard*.

Summary of the DoD's Accountability and Accounting Systems. Section V presents a summary discussion of the Military Departments' ND PP&E accountability and accounting systems, which describes the capabilities of the various systems for implementing the recommended standard.

Implementation Issues, Cost Estimates and Timelines and Audit Issues. Section VI presents a discussion of implementation issues, the estimated costs for implementing the proposed standard and timelines. Section VII discusses audit issues associated with the recommended standard and how these issues should be addressed.

Appendices. Appendices supplement the report. Appendix A - *Recommended Definition and Standard*, provides a proposed revised ND PP&E definition and a proposed revised standard on accounting and reporting. Appendix B - *Financial Reporting Objectives*, includes a listing of the FASAB, FASB, and GASB financial reporting objectives, derived from their respective concepts statements. Appendix C - *Discussion of User Comments*, provides a detailed discussion of the results of the user surveys. Appendix D - *DoD's Accountability and Accounting Systems*, describes the DoD's ND PP&E accountability and accounting systems in detail. Appendix E - *Components of Full Cost*, includes a description of the elements of cost that could be included in the definition of Full Cost. Finally, Appendix F - *Acronyms*, includes definitions of acronyms used in this report.

Section II – Summary of the ND PP&E Acquisition Process

To understand the context of KPMG's recommendation, it is important to understand the complexities of both the DoD's acquisition process and ND PP&E acquisition programs. This section summarizes KPMG's Defense Acquisition Management System Tutorial dated June 9, 2000, and briefly describes the process and highlights a major acquisition program to illustrate the system's complexity.

ND PP&E acquisition is more than just the procurement of goods and services to meet a particular need. It is a lengthy and complex process that includes the conceptualization, design, research, development, test and evaluation, production, and procurement of a weapon system or major system component. The DoD associates the costs of these activities with an ND PP&E acquisition program, not with individual items of ND PP&E. ND PP&E acquisition program cost information is used for program monitoring by Congress, DoD management, and others (e.g., OMB, CBO, GAO).

ND PP&E Acquisition Program

An ND PP&E acquisition program is designed to provide a new, improved, or continuing weapons system capability in response to an operational need. The DoD categorizes ND PP&E acquisition programs according to size and complexity. The acquisition category (ACAT) designation is based upon an estimate of program costs or is assigned by senior DoD acquisition officials and is an important determinant of acquisition program reporting requirements. ACAT I programs, referred to as Major Defense Acquisition Programs, are programs estimated to require total expenditures of \$355 million for Research, Development, Test, and Evaluation (RDT&E), or \$2.135 billion for Procurement, both in 1996 constant dollars. ACAT II programs are acquisition programs estimated to require total expenditures of more than \$135 million for RDT&E, or more than \$640 million for Procurement, both in 1996 constant dollars. ACAT III and IV programs consist of all other acquisition programs. ACAT II – IV acquisition programs may be managed in a manner different from the management of ACAT I programs.

Acquisition Support Framework

The DoD's acquisition support framework is comprised of three primary decision support processes: (1) requirements generation, (2) planning, programming and budgeting, and (3) acquisition management. These processes function concurrently.

Requirements Generation

The requirements generation process produces information for decision-makers on mission needs. This process is comprised of several outputs, including a Mission Area Analysis (MAA), a Mission Need Statement (MNS), an Analysis of Alternatives (AoA), and an Operational Requirements Document (ORD).

The MAA is an assessment of the capabilities of the current force structure (people and materiel), taking into account opportunities for technological advancement, cost savings, and changes in national defense policy. The MAA results in a determination of mission needs. The

MNS describes an operational capability need in broad operational terms rather than system specific terms. It seeks to identify deficiencies and technological opportunities on a continual basis in order to provide materiel and non-materiel solutions to national security issues. The AoA gauges the cost and operational effectiveness of possible alternatives for meeting deficiencies or opportunities identified in the MNS. It aids the decision-making process by highlighting the advantages and disadvantages of various system alternatives. The ORD describes the system solution in terms of the operational performance requirements necessary to satisfy the mission need.

Planning, Programming, and Budgeting

The DoD planning, programming, and budgeting process is supported by the Planning, Program, and Budgeting System (PPBS), which is a formal systematic structure for making decisions on policy, strategy, and the development of forces and capabilities to accomplish anticipated missions. It is a calendar-driven, cyclical-process containing three distinct but interrelated phases: planning, programming, and budgeting. These produce the DoD portion of the President's Budget.

The foundation of the PPBS is the Future Years Defense Program (FYDP). The DoD prepares and manages its financial plan in the context of the FYDP. The FYDP is a plan that addresses all forces and resources associated with programs approved by the Secretary of Defense and is used for internal DoD planning purposes. The FYDP information structure captures data by the Military Departments, Major Force Program, which represents a macro-level force mission or support mission (e.g., Strategic Forces, Airlift and Sealift), and appropriation category.

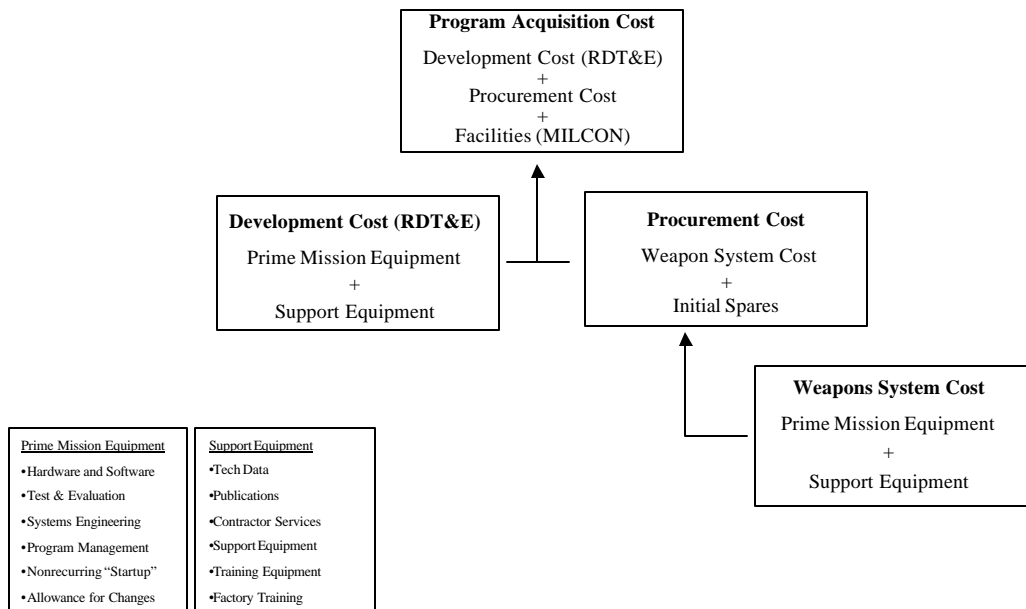
The primary *appropriation categories* include RDT&E, Procurement, Operations and Maintenance (O&M), Military Personnel (MILPERS), and Military Construction (MILCON).

RDT&E appropriations fund basic and applied research, including prototyping, testing, and evaluation. Procurement appropriations fund the acquisition of ND PP&E, which includes weapons systems, initial spares, and costs to deliver an operational end item. Individual Military Department rules govern the use of funds in support of field modifications to existing ND PP&E. O&M appropriations fund operating costs, civilian salaries, travel, fuel, training and education, base operations support, and recruiting. MILPERS appropriations fund pay and allowances for active duty and reserve military personnel as well as retirement pay. MILCON appropriations fund military construction projects, which may be associated with a specific type of ND PP&E.

Acquisition Management

The acquisition management process involves the management of all phases of the acquisition life cycle, a four-phase process that includes concept exploration, program definition and risk reduction, engineering and manufacturing, and production, fielding/deployment and operational support. The process involves managing numerous program cost components, e.g., RDT&E, Procurement, and systems specific MILCON, the sum of which represent Program Acquisition Costs, described in Exhibit A below.

Exhibit A, Components of Program Acquisition Cost



ND PP&E Acquisition Reporting

ND PP&E acquisition reporting is designed primarily for internal management oversight and Congressional oversight of Major Defense Acquisition Programs. This activity involves multiple reports designed to provide information for monitoring the acquisition process. The following reports are relevant to the ND PP&E reporting evaluation process:

Selected Acquisition Report (SAR)

The SAR is a statutorily-required, comprehensive status report on Major Defense Acquisition Programs (MDAP). The primary objective of the SAR reporting requirement is to obtain consistent, reliable data on the status of ACAT I programs. The SAR provides program status information, such as schedule and weapon system capability statistics, and financial information. It contains one element of actual cost – expenditures to date.

Defense Acquisition Executive Summary (DAES)

The DAES provides progress information to the DoD principals on selected acquisition programs. DAES is an internal DoD report whose primary users are the Defense and Service Acquisition Executives. Similar to the SAR, the DAES covers ACAT I programs. The DAES reports program assessments, unit cost, current estimates of the program parameters, exit criteria status, and vulnerability assessments. The DAES presents a projection of total costs and quantities through the end of the acquisition phase.

Budget Execution Reports

Each Service tracks obligations and outlays using Service specific systems and issues budget execution reports that reflect obligations and outlays. Financial data is captured at the appropriation and program element levels.

Complexity of Acquisition Programs

The following discussion illustrates the complexity of ND PP&E acquisition programs and the associated acquisition process. It describes the acquisition process relating to the DDG 51 class of destroyers, known as the AEGIS Destroyer, included in our report on the ND PP&E acquisition process.

The DDG 51 acquisition program is comprised of numerous systems and sub-systems, each of which is classified by ACAT depending on total cost. In total, there are 81 ACAT programs that produce systems and sub-systems included on the DDG 51: 13 in ACAT I, 13 in ACAT II, 10 in ACAT III, 10 in ACAT IV, and 35 in non-ACAT programs. All of the integration, procurement, installation, and testing for these systems and sub-systems are budgeted and paid for out of the DDG 51 acquisition program procurement line item or appropriation. However, the funding for RDT&E related to some of these ACAT programs is separate from the funding for the DDG 51 program.

The DoD currently plans to acquire 58 ships by end of 2010. The first ship was constructed in 1985, and the Navy currently has 29 DDG 51 ships.

Total cost of the DDG 51 acquisition program is estimated at \$54 billion. This estimate does not include the cost of post-fielding modifications or operating and support costs. In addition, the Navy plans to spend in excess of \$22 billion on DDG 51 post-fielding modification over a 56-year period.

There are several models or “flights” of the DDG 51. Each flight number has different features and capabilities, such as the hull structure, aviation facilities, mechanical systems, communication systems, weapons systems, and combat systems.

For DDG 51 ships already in use, some existing features and capabilities will be modified through the post-fielding modification process to provide for the improved features and capabilities of new flights. However, not all existing ships will be modified due to cost constraints and technical considerations. The post-fielding modification process is not simply replacing components. Some post-fielding modifications relate to changes to the ship, such as improvements to the hull structure and solid waste management system. Other changes relate to components, for example, deletion of the Close-In Weapons System and Harpoon Missile System and the addition of the Sea Sparrow Missile System. Given that replaced components were included in the total acquisition cost of the DDG 51 program, it would be extremely difficult, if not impossible, to value components replaced as part of the post-fielding modification process.

The accounting for the DDG 51 program is an extremely complex process. It involves numerous contracts and the tracking of hundreds, if not thousands, of related, complex contract line items

and related obligation and outlay transactions over a long period of time, all of which are associated with the DDG 51 acquisition program. The accounting complexities extend to the post-fielding modifications process, which also accounts for the total acquisition cost of the modification program.

Cost information is captured in multiple transaction processing systems, which provide ND PP&E program acquisition cost information to central accounting systems (the Standard Accounting and Reporting System for the Navy). Such cost information is the accumulation of thousands of progress payments for numerous contract line items over the life of the acquisition program. The central accounting system provides information used in producing consolidated budget execution reports and program budget execution reports on acquisition programs. These systems are also the primary source of information on acquisition programs for the SAR and DAES reporting.

Conclusion

ND PP&E acquisition is a long-term, complex process that involves accounting for the cost of RDT&E, Procurement, and facilities as well as accounting for the cost of ND PP&E modifications and upgrades. The acquisition process associated with these components involves hundreds if not thousands of contract line items and related transactions. The DoD accounts for these costs as ND PP&E acquisition program costs. The systems used to collect this information provide the total ND PP&E acquisition program cost data reported to Congress and others.

* * * * *

While the DoD has historically reported the costs of acquisition programs for internal management and Congressional oversight, general-purpose financial statements are intended to satisfy the information needs of a broader audience, including Congress, program managers, other government executives, and citizens. The analysis of the objectives of financial reporting and the needs of users, which follows, provides the basis for assessing the relevance of existing FASAB ND PP&E accounting and reporting requirements and proposed revisions to these requirements. In addition, the analysis concludes with KPMG's recommended ND PP&E accounting and reporting approach that is intended to address the financial reporting objectives and user needs discussed herein and the reasons for our recommendation.

Section III – Summary of Financial Reporting Objectives

Introduction

The American Institute of Certified Public Accountants defines generally accepted accounting principles as those issued by three standards setting bodies: the Federal Accounting Standards Advisory Board (FASAB), the Financial Accounting Standards Board (FASB), and the Governmental Accounting Standards Board (GASB). The FASAB issues standards for the federal government, the FASB issues standards for private sector business enterprises and non-business organizations, and the GASB issues standards for state and local governments. These bodies have issued concepts statements, which establish the objectives of financial reporting for their constituencies, to guide their efforts in setting standards.

The FASAB prescribed the objectives of federal financial reporting in Statement of Federal Financial Accounting Concepts (SFFAC) Number 1, *Objectives of Federal Financial Reporting*. The FASAB provided that SFFAC Number 1 will guide its work to ensure that future standards are consistent with the objectives articulated therein and assist it in dealing with the special circumstances of the federal government in a way that meets users' needs for information. FASAB identified users as the citizenry, the Congress, and federal executives and program managers.

The FASB prescribed the objectives of financial reporting for business enterprises and non-business organizations in Statements of Financial Accounting Concepts Number 1, *Objectives of Financial Reporting by Business Enterprises*, and Number 4, *Objectives of Financial Reporting by Nonbusiness Organizations*. The FASB stated that the objectives of financial reporting by business enterprises are based on the information needs of present and potential investors and creditors and other users in making rational investment, credit, and similar decisions. Furthermore, it states that the objectives of financial reporting by nonbusiness organizations are based on the information needs of present and potential resource providers and other users in making rational decisions about the allocation of resources to these organizations.

The GASB prescribed the objectives of financial reporting for state and local governments in Concepts Statement Number 1, *Objectives of Financial Reporting*. The GASB concepts statement provides that financial reporting should assist in: (1) fulfilling government's duty to be publicly accountable, (2) evaluating operating results, and (3) assessing the level of services that can be provided and an entity's ability to meet obligations as they become due.

KPMG presents a detailed discussion of these concepts statements in Appendix B - *Financial Reporting Objectives*.

Given the stated purpose of the objectives, KPMG concluded that the evaluation of existing and proposed standards for reporting ND PP&E should be based on the objectives as well as the needs of the user community.

ND PP&E reporting does not provide information relevant to all of the foregoing objectives. The discussion that follows focuses on the objectives issued by the FASAB and related

objectives issued by the FASB and the GASB and the relevance of the various ND PP&E reporting approaches to achieving these objectives. The purpose of this analysis is to assess the effectiveness of various ND PP&E reporting approaches in providing the information needed to meet the relevant objectives.

Reporting Objectives Relevant to ND PP&E

Budgetary Integrity

The first category of objectives issued by the FASAB pertains to budgetary integrity. This objective provides that financial reporting should provide information that helps the reader determine: (1) how budgetary resources have been obtained and used, whether the use was in accordance with the legal authorization, (2) the status of budgetary resources, and (3) how budgetary information relates to information on the costs of programs and whether information on the status of budgetary resources is consistent with the accounting information on assets and liabilities. The intent of these objectives is to stress the importance of budgetary reporting and the need to reconcile operating information presented on a budgetary basis with operating information presented on another basis, for example, the accrual basis of accounting.

ND PP&E financial reporting approaches discussed in this evaluation would not provide information about the status of budgetary resources or how the use of budgetary resources relates to the costs of programs. Information on the status of budgetary resources would only be provided through budgetary comparison reporting. With respect to providing information about how budgetary resources relate to the cost of programs, federal financial reporting requirements provide for the reconciliation of budgetary and cost information at the entity, rather the program-level. Reasons for differences are explained in the notes to federal entity financial statements. Differences between the accounting for, and reporting of, ND PP&E for financial statement and budgetary reporting would be included in the required reconciliation and note disclosures.

For financial reporting of ND PP&E to provide information about whether the DoD used the budgetary resources in accordance with legal authorization, reported ND PP&E information would have to be consistent with the information reported for budgetary monitoring. Specifically, the definition of ND PP&E and associated accounting requirements would need to be consistent with the definition used for budgetary purposes and the information reported would have to be consistent with the information reported for budgetary monitoring. Any material differences would have to be disclosed.

If the definition of ND PP&E for financial reporting is materially inconsistent with the definition used for budgetary monitoring, and the financial reporting requirements for ND PP&E are materially inconsistent with budgetary accounting requirements, then the reporting approaches discussed herein will not provide information necessary to assist users in determining whether resources were used in accordance with legal authorization.

Operating Performance

The second FASAB reporting objective category pertains to operating performance. SFFAC Number 1 provides that federal financial reporting should assist report users in evaluating the service efforts, costs, and accomplishments of the reporting entity, the manner in which these efforts and accomplishments have been financed, and the management of the entity's assets and liabilities. With respect to accounting for, and reporting of, ND PP&E, information to achieve this objective includes that which helps the reader to determine:

- the costs of providing specific programs and activities and the composition of, and changes in, these costs.
- the efficiency and effectiveness of the government's management of its assets and liabilities.
- the efforts and accomplishments associated with federal programs and the changes over time and in relation to costs.

Related FASB objectives for business enterprises and non-business organizations include providing information about:

- a business enterprise's financial performance during a period.
- the performance of a non-business organization during a period. Periodic measurement of the changes in the amount and nature of the net resources of a non-business organization and information about the service efforts and accomplishments of an organization together represent the information most useful in assessing its performance.
- the service efforts of a non-business organization.
- the service accomplishments of a non-business organization.
- the services that a non-business organization provides and its ability to continue to provide those services.

The related GASB objective addresses providing information to assist users in assessing the service efforts, costs, and accomplishments of the governmental entity.

Stewardship

The third FASAB reporting objective category pertains to stewardship. SFFAC Number 1 provides that federal financial reporting should assist report users in assessing the impact on the country of the government's operations and investments for the period and how, as a result, the government's and the nation's financial condition have changed and may change in the future. With respect to the accounting for, and reporting of, ND PP&E, information to achieve this broad objective includes that which helps the reader to determine whether:

- the government's financial position improved or deteriorated over the period.
- government operations have contributed to the nation's current and future well being.

Related FASB objectives for business enterprises and non-business organizations include providing information about:

- the economic resources of a business enterprise, the claims to those resources (obligations of the enterprise to transfer resources to other entities and owners' equity), and the effects of transactions, events, and circumstances that change resources and claims to those resources.
- a business enterprise's economic resources, obligations, and owners' equity.
- how management of a business enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it.
- how managers of a non-business organization have discharged their stewardship responsibilities and about other aspects of their performance.

Related GASB objectives for state and local government entities include providing information about physical and other non-financial resources having useful lives that extend beyond the current year, including information that can be used to assess the service potential of those resources.

Systems and Controls

The fourth category of FASAB objectives pertains to systems and controls. The systems and controls objective provides that federal financial reporting should assist report users in understanding whether financial management systems and internal accounting and administrative controls are adequate to ensure that transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purpose authorized, and recorded in accordance with federal accounting standards.

Management is responsible for ensuring that systems and controls are sufficient to achieve these objectives. Financial reporting alone does not assist users of federal financial reports in understanding whether management has implemented the appropriate systems and controls. It follows then that this objective requires management to explicitly report on the adequacy of an entity's systems and controls for achieving the systems and control objectives. This reporting requirement is contained in the Federal Managers Financial Integrity Act and in SSFAS Number 15, *Management's Discussion and Analysis*.

This objective does not affect the reporting of financial information, such as ND PP&E, but rather presumes a report by management on the adequacy of systems and controls. Therefore, it is not relevant to the discussion of various ND PP&E reporting approaches.

It is important to understand the assertions embodied in amounts presented on financial statements and in management's report on systems and controls. It is also important to understand the relevance of each assertion in terms of the various reporting approaches discussed in this section. The financial reporting assertions are: (1) existence or occurrence, (2) completeness, (3) rights and obligations, (4) valuation or allocation, and (5) presentation and disclosure. The relevance of each in terms of ND PP&E reporting is included in the assessment of the various reporting approaches, which follows.

User Needs

As stated in SFFAC Number 1, the mission of FASAB is to recommend accounting standards after considering the financial and budgetary information needs of users of federal financial information. FASAB and its sponsors believe that federal financial reporting standards should consider the decisional needs of both internal and external report users.

This implies a different role for FASAB than for FASB and GASB. Both the FASB and GASB exist primarily to set standards for general purpose financial reporting for use primarily by parties external to the reporting entity. The FASB and GASB do not need to weigh heavily managers' information needs because those individuals, by definition, are assumed to have ready access to the information they need about the financial transactions and events that affect the financial position, and operations they manage. As stated in SFFAC Number 1, paragraph 25:

...the distinction between internal and external users is in many ways less significant for the federal government than for other entities. Officials who in theory should have ready access to information often find in practice that it is not available. Factors that contribute to this problem include the size and complexity of the government, the rapid turnover among senior political executives compared with the time required to install information systems in large bureaucracies, and the division of authority in the federal government.

SFFAC Number 1, classifies users of federal financial reports into four major groups: citizens, Congress, executives, and program managers. SFFAC Number 1 describes each of these groups as follows:

- Citizens - This group includes taxpayers, voters, service recipients, news media, public interest and other advocacy groups, state and local legislators and executives, and analysts from corporations, academe, and elsewhere. Citizens are primarily concerned with individual programs, the services the government provides, the outputs and outcomes of those services and the efficiency with which services are provided, and with fiscal responsibility.
- Congress - This group includes elected members of Congress and Congressional staff, and the Congressional Budget Office and the General Accounting Office. This group is concerned with broad policies, priorities, and the programs that implement those priorities.

- Executives - This group includes the President and those acting as his agents, such as agency heads, other senior executives, and central agency officials in OMB and the Department of the Treasury. Executives, like Congress, are concerned with the government's priorities and the programs that implement those priorities.
- Program Managers - This group includes individuals who manage government programs. Their concerns include operating plans, program operations, and budget execution.

KPMG, working with the DoD and the FASAB staff, identified users of, and other parties interested in, information about ND PP&E, federal financial statements, and federal financial management improvement efforts. KPMG interviewed fourteen individuals that included representatives from each of the groups described above as follows:

- Citizens - This group consisted of four individuals, one from each of the following communities: academe, non-FASAB standards setting body, a research organization, and a private sector organization.
- Congress - This group was comprised of four individuals including two Congressional staff representatives, one Congressional Budget Office representative, and one General Accounting Office representative.
- Executives - This group included one central agency senior executive.
- Program Managers - This group consisted of five DoD senior executives.

The objectives of financial reporting are designed to guide the FASAB in developing accounting standards to enhance the financial information reported by the federal government to: (1) demonstrate its accountability, (2) provide useful information, and (3) help internal users of financial information improve the government's management. To obtain a user perspective, we interviewed individuals from the foregoing groups about the usefulness of the following ND PP&E reporting approaches:

- Capitalization of ND PP&E either on the balance sheet or as RSSI.
- Estimated loss in value of ND PP&E.
- Quantity and condition of ND PP&E.
- Actual versus planned ND PP&E investment information.

KPMG also asked the users about the importance of audited ND PP&E information. KPMG prepared a survey that included questions relating to the usefulness of the ND PP&E reporting approaches discussed above, provided the questionnaire in advance of formal discussions, and interviewed survey participants. A summary of the results of these interviews is contained in Section IV – *Financial Reporting Approaches, Recommendation, and Basis for Conclusion*. A detailed discussion is contained in Appendix C – *Discussion of User Comments*.

Section IV – Financial Reporting Approaches, Recommendation, and Basis for Conclusion

Introduction

The DoD asked KPMG to evaluate four ND PP&E reporting approaches and to recommend a ND PP&E accounting and reporting standard that would provide users of the DoD's financial statements with ND PP&E information that is meaningful and has analytical utility. This section: (1) describes the various ND PP&E accounting and reporting approaches, (2) compares each alternative with the operating performance, stewardship, and systems and controls, and (3) compares the approaches with user needs. We discuss the relevance of the budgetary integrity objective in the preceding section, thus we do not discuss it in this section. The purpose of this comparison is to determine whether, and, in what way, each approach assists in satisfying the objectives and the needs of users of federal financial statements.

Description of the Reporting Approaches

The following paragraphs provide a brief summary of four potential accounting and reporting approaches for ND PP&E.

Capitalizing and Reporting ND PP&E on the Balance Sheet

Capitalization involves the accounting for, and reporting of, costs that provide future economic benefit or service potential to an organization. In contrast with budgetary reporting, these costs are not reported as expenses when incurred, but rather, they are expensed in future periods if ² and when the economic resource is consumed or the service potential is lost. Accordingly, under this alternative, ND PP&E costs would be capitalized when incurred and expensed in future periods.

Capitalizing and Reporting ND PP&E as RSSI

Required Supplementary Stewardship Information (RSSI) is unique to federal financial reporting. RSSI relates to reporting information about resources that are not defined as assets and, accordingly, are not included in financial statements.

RSSI information does not meet the definition of assets, but is important to understanding the financial condition of the federal government. Capitalization of ND PP&E as RSSI involves the accounting for, and reporting of, costs of acquisition programs (e.g., DDG 51 program), classes of ND PP&E (e.g., warships), or types of ND PP&E (e.g., DDG 51) that provide future economic benefit or service potential to an organization in a form that supplements the basic financial statements. In contrast with the balance sheet approach, under this approach the basic

² The term "if" is used because a capitalized economic resource might not be consumed and/or the service potential might not be lost.

financial statements report the costs of ND PP&E as expenses when incurred rather than when the associated economic resource is consumed or service life lost.

Reporting Units of ND PP&E as RSSI

Reporting units of ND PP&E as RSSI involves the accounting for, and reporting of, ND PP&E quantity information. This presentation represents the physical quantities of ND PP&E that provide a future economic benefit or service potential rather than the costs that benefit future periods. In contrast with the balance sheet approach, but as with other forms of RSSI reporting, under this alternative the basic financial statements report the costs of ND PP&E as expenses when incurred rather than when the associated economic resource is consumed or service life lost.

Reporting ND PP&E Investments as RSSI

Reporting investments in ND PP&E as RSSI involves the reporting of current year and cumulative expenses associated with ND PP&E acquisition programs. This approach would provide information similar to capitalizing and reporting ND PP&E as RSSI, except that it would report discretely current period costs that benefit future periods. In contrast with the balance sheet approach, but as with other forms of RSSI reporting, under this approach the basic financial statements report the costs of ND PP&E as expenses when incurred rather than when the associated economic resource is consumed or service life lost.

Comparison of Approaches with Financial Reporting Objectives

We compared each of the four approaches with the Financial Reporting Objectives to determine the extent to which each approach satisfied the objectives.

Capitalizing and Reporting ND PP&E on the Balance Sheet

Operating Performance

The operating performance objective provides that financial reporting should assist the reader of financial statements in determining the costs of specific programs (missions in military terms), the efficiency and effectiveness of the government's management of its assets, and the efforts and accomplishments and the changes over time in relation to costs.

The definition of performance is a prerequisite to evaluating whether a particular reporting option assists in providing the information necessary to measure the associated costs. For example, if performance is measured in terms of procurement, then the traditional approach of capitalization and depreciation is not an effective reporting approach. However, if performance is measured in terms of the missions of an entity, and ND PP&E is used in performing these missions, or in terms of asset management, then capitalization is an effective measurement tool.

For the purposes of assessing whether capitalization of ND PP&E will provide the information necessary to satisfy this objective, we defined performance in terms of the efforts expended by the Military Departments in accomplishing their respective missions and asset management.

Given this definition, the capitalization of ND PP&E provides the information necessary for allocating the investment in ND PP&E to the missions and over the benefiting periods, assessing the availability of resources for use in support of missions in future periods, and for assessing how well management used resources provided for ND PP&E.

Stewardship

The stewardship objective addresses the need to provide information that will assist users in determining whether the government's financial position improved or deteriorated and whether the government's operations have contributed to the nation's well being. Related FASB objectives address this in terms of economic resources³ of a business enterprise.

ND PP&E by design has a long-term service potential and provides a future economic benefit. Accordingly, capitalization of ND PP&E contributes to a determination of whether the government's financial position improved or deteriorated over time. Failure to capitalize ND PP&E results in an understatement of the government's economic resources and financial position.

Systems and Controls

Capitalizing and reporting ND PP&E on the balance sheet enables management to make the following assertions:

- Existence or occurrence – Reported ND PP&E exists.
- Completeness – All ND PP&E transactions and other events and circumstances that occurred and should have been recognized have been recorded and reported.
- Rights and obligations – Recorded and reported ND PP&E belong to the DoD.
- Valuation or allocation – ND PP&E is recorded and reported at appropriate amounts in conformity with relevant and appropriate accounting principles. Transactions are mathematically correct and appropriately summarized, and recorded in the DoD's financial statements.
- Presentation and disclosure – ND PP&E reported in the financial statements is properly described, sorted, and classified.

Capitalizing and Reporting ND PP&E as RSSI

The objective of RSSI is to report resources that involve substantial investment by the federal government for the benefit of the nation. Investments reported as RSSI provide long-term benefits to the nation. Reporting these investments highlights that they have a long-term benefit

³ *The common characteristic possessed by all assets (economic resources) is "service potential" or "future economic benefit," the scarce capacity to provide services or benefits to the entities that use them as defined in Statement of Financial Accounting Concepts Number 6, "Elements of Financial Statements."*

and demonstrates accountability over them. These investments are also reported as expenses in the period in which the expenses are incurred.

Operating Performance

Under this reporting approach period costs would be limited to the costs of operating and maintaining ND PP&E. There is an argument in favor of limiting period costs to the costs of operating and maintaining ND PP&E. This argument focuses primarily on the belief that ND PP&E has an indeterminate or unpredictable useful life due the continuous nature of modifications, improvements, and maintenance. Moreover, ND PP&E must be maintained in a constant state of readiness to perform its designated mission. To the extent that ND PP&E is maintained in a state of readiness similar to when the asset was new, a strong case can be made that it has not lost value due to use.

GASB recently recognized this concept in Statement Number 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*. The GASB provided that state and local governments did not have to depreciate infrastructure assets if these governments meet certain criteria, the principal one being that infrastructure is preserved at the condition level established and disclosed by the government.

If this principle applied to ND PP&E, this reporting objective would be met by virtue of the fact that operating and maintenance costs would be an appropriate measure of ND PP&E operating performance. However, in contrast to the GASB concept in Statement Number 34, this reporting approach does not provide for capitalizing the cost of ND PP&E on the balance sheet, thus both the current investment in ND PP&E and current operating and maintenance costs are recognized and reported as current costs on the Statement of Net Costs, overstating expenses and net costs for the period.

Stewardship

Under the RSSI reporting method the costs associated with acquiring ND PP&E are expensed when incurred and captured and reported as RSSI. This form of reporting accomplishes one objective relevant to this study; it provides information about economic resources. The current FASAB standard applicable to ND PP&E requires that the DoD report changes in the value of ND PP&E resulting from additions and deletions during the year and the balance at the end of the year. This latter amount should equal the amount capitalized under the balance sheet method. Accordingly, while not included on the balance sheet, this form of reporting would provide the same information and satisfy the stewardship objective concerning providing information about how the financial position improved or deteriorated.

Systems and Controls

Capitalizing and reporting ND PP&E as RSSI enables management to make the following assertions:

- Existence or occurrence – Reported ND PP&E exists.
- Completeness – All ND PP&E transactions and other events and circumstances that occurred and should have been recognized have been recorded and reported.
- Rights and obligations – Recorded and reported ND PP&E belong to the DoD.
- Valuation or allocation – ND PP&E is recorded and reported at appropriate amounts in conformity with relevant and appropriate accounting principles. Transactions are mathematically correct and appropriately summarized, and recorded in the DoD's financial statements.
- Presentation and disclosure – ND PP&E reported in the financial statements is properly described, sorted, and classified.

Reporting Units of ND PP&E as RSSI

Operating Performance

Accounting concepts and standards have few references to the reporting of quantify information alone. The objectives address operating performance in monetary terms, with the exception of information on outputs and outcomes, and they provide for the reporting of this information in relation to costs.

The primary reference to quantity information is in discussions of service efforts and accomplishments, principally in terms of program outputs. Quantity or output information is an important ingredient for performance measurement in non-business entities given the necessary focus on non-financial operating performance whereas net income or the “bottom line” is considered as one of the important measures of business enterprise operating performance.

With respect to ND PP&E, unit reporting could provide a basis for measuring operating performance if used to supplement other reporting approaches. As discussed in the section on capitalizing ND PP&E on the balance sheet, capitalization provides the means for measuring operating performance in terms of the efforts expended by the Military Departments in accomplishing their respective missions. Unit reporting provides information about the resources acquired and on-hand to accomplish the DoD's missions solely in terms of outputs.

Reporting ND PP&E solely in terms of units would not provide data necessary for measuring operating performance from an efforts expended perspective nor would it provide sufficient information for measuring performance from a resources acquired perspective. To effectively evaluate the former, one needs information appropriate for measuring the cost of providing services. To effectively evaluate the latter, one needs information about the total costs of assets acquired (outputs) and possibly other information, such as expected outputs given the extensive “up-front” costs associated with ND PP&E prior to delivery of physical assets.

Accordingly, unit information alone does not assist in achieving the operating performance objective, whether measured in terms of mission costs or the effectiveness of the acquisition process.

Stewardship

The stewardship objective focuses on financial resources in the context of whether the financial position improved or deteriorated and operations contributed to the nation's current and future well-being. Related objectives for reporting by non-business organizations issued by the FASB also provide for the reporting of information that enable users to assess how managers have discharged their stewardship responsibilities.

It is difficult to see how unit reporting can provide information relevant to an assessment of financial position. Unit reporting may, however, provide information about how effectively management discharged its stewardship responsibilities and, in turn, about how these investments contributed to the future well-being of the nation. For example, unit information may assist users in assessing the capacity of a program to accomplish its objectives. Management may have invested resources for their intended purpose but the unit data may assist users in assessing whether the number produced or expected to be produced is sufficient to accomplish program objectives.

Accordingly, reporting of the unit information does not address effectively the financial position component of the stewardship objective; however, it may facilitate an assessment management's stewardship and how the program contributed to the nation's well being.

Systems and Controls

Reporting units of ND PP&E as RSSI enables management to make the following assertions:

- Existence or occurrence – Reported ND PP&E exists.
- Completeness – All ND PP&E transactions and other events and circumstances that occurred and should have been recognized have been recorded and reported.
- Rights and obligations – Recorded and reported ND PP&E belong to the DoD.
- Valuation or allocation – Not applicable.
- Presentation and disclosure – ND PP&E reported in the financial statements is properly described, sorted, and classified.

Reporting ND PP&E Investments as RSSI

Reporting ND PP&E investments includes information about current year ND PP&E program expenses (additions), reductions in the investments in ND PP&E during the year, and the balance of the investments in ND PP&E at the end of the year. The objective of this presentation is to provide users with information in a form similar to that used currently to monitor program costs and other activity from a budgetary perspective.

Operating Performance

As with the approach for reporting the capitalizable amount as RSSI, under this approach investments in ND PP&E are reported as expenses in the period incurred and ND PP&E operating costs are limited to operating and maintenance expenses – depreciation is excluded. The argument in favor of limiting period costs to the costs of operating and maintaining ND PP&E is the same as discussed under the approach for capitalizing ND PP&E as RSSI. Specifically, the DoD must maintain ND PP&E in a state of constant readiness in order to perform its mission. Therefore, it is being continuously maintained, modified, and improved and, accordingly, has not lost value due to use. As previously discussed, the GASB provided that state and local governments did not have to depreciate infrastructure assets if these governments met certain criteria, the principal one being that infrastructure is preserved at the condition level established and disclosed by the government.

If this principle applied to ND PP&E, this reporting objective would be met by virtue of the fact that operating and maintenance costs would be an appropriate measure of ND PP&E operating performance. However, in contrast to the GASB concept in Statement Number 34, this reporting approach does not provide for capitalizing the cost of ND PP&E. This current investment in ND PP&E and the current operating and maintenance costs are reported as expenses on the Statement of Net Costs. As a result, expenses and net costs for the period are overstated.

Stewardship

This reporting approach provides much of the same information required to satisfy the stewardship objective that is provided by the approach requiring capitalization on the balance sheet or reporting of the same information as RSSI. As with these other approaches, this approach provides information useful for assessing whether the government's financial position improved or deteriorated during the year.

Systems and Controls

Reporting investments in ND PP&E as RSSI enables management to make the following assertions:

- Existence or occurrence – Reported ND PP&E exists.
- Completeness – All ND PP&E transactions and other events and circumstances that occurred and should have been recognized have been recorded and reported.
- Rights and obligations – Recorded and reported ND PP&E belong to the DoD.
- Valuation or allocation – ND PP&E is recorded and reported at appropriate amounts in conformity with relevant and appropriate accounting principles. Transactions are mathematically correct and appropriately summarized, and recorded in the DoD's financial statements.
- Presentation and disclosure – ND PP&E reported in the financial statements is properly described, sorted, and classified.

Comparison of Approaches with User Needs

The following table summarizes the views of users and other interested parties about the usefulness of the capitalized cost of ND PP&E, estimated loss in ND PP&E value, ND PP&E quantity information, and planned versus actual investment information. The table also summarizes the views concerning the importance of audited ND PP&E information.

Table IV-I

	Citizen	Congress	Executive	Program Managers	Summary
Capitalization	4 useful	2 useful 2 not useful	1 useful	1 useful 4 not useful	8 useful 6 not useful
Estimated Loss In Value (Depreciation)	3 useful 1 not useful	2 useful 2 not useful	1 useful	5 not useful	6 useful 8 not useful
Condition	2 useful 2 not useful	4 useful	1 useful	4 useful 1 not useful	11 useful 3 not useful
Quantity	2 useful 2 not useful	4 useful	1 useful	4 useful 1 not useful	11 useful 3 not useful
Planned versus Actual Investment Information	3 useful 1 not useful	3 useful 1 not useful	1 useful	4 useful 1 not useful	11 useful 3 not useful
Importance of Audit	4 useful	4 useful	1 useful	5 useful	14 useful

A detailed discussion of the results of our user survey is contained in Appendix C - *Discussion of User Comments*. As reflected in the table, a majority of those surveyed indicated that capitalization of ND PP&E was useful information. A majority of those surveyed also indicated that information relating to ND PP&E condition, quantities, and planned versus actual investments was useful information. Lastly, all of those surveyed indicated that an audit of ND PP&E information was useful. A minority of those surveyed felt information about a loss in ND PP&E value (depreciation) would be useful.

Conclusion

Based on the foregoing analysis, which is summarized below, KPMG concludes that no single reporting approach from those described above provides the information necessary to satisfy the reporting objectives and the needs of the entire user community.

The approach of capitalizing the cost of ND PP&E and reporting it on the balance sheet provides the information or a basis for measuring operating performance and assessing stewardship. However, it does not facilitate assessing budgetary integrity or systems and controls.

The approaches of reporting the capitalizable cost of ND PP&E and the current and cumulative investment in ND PP&E as RSSI, the latter at the acquisition program level for certain major acquisition programs, also provide information for assessing stewardship. Both approaches present the same or amounts similar to the balance sheet approach. However, neither approach provides the information necessary for assessing systems and controls and both impede the DoD's ability to measure operating performance, since under both approaches the annual cost of

operations would include the costs of acquisition programs, i.e., annual acquisition costs would be expensed and the annual cost of operations would be overstated.

With respect to budgetary integrity, reporting of investment information by major ND PP&E acquisition program provides information for assessing these programs from a planning or budgetary perspective. Users expressed a preference for a presentation of planned acquisition program cost information. However, given the life and complexity of an ND PP&E acquisition program and events, such as significant technological changes and modifications that occur during the acquisition life-cycle and political support for an acquisition program, this information could be subject to varying interpretations absent explanation. Accordingly, consideration should be given to methods for ensuring consistent interpretation.

The majority of users expressed the belief that the reporting of capitalizable cost information in general, regardless of whether the information was presented on the balance sheet or as RSSI, was important as ND PP&E represents an economic resource that has future service potential.

Unit reporting does not provide a basis for assessing budgetary integrity, operating performance, stewardship, or systems and controls. Monetary information is needed to assess operating performance, stewardship, and budgetary integrity. Moreover, accounting concepts and standards have few references to the reporting of quantity information alone. The principal reference is in discussions of service efforts and accomplishments, principally in terms of program outputs.

With respect to condition information, the majority of users viewed quantity and condition information as useful. They expressed the opinion that a combination of quantity and condition information will assist readers in assessing military readiness and ND PP&E accountability.

In consideration of the foregoing, KPMG developed an alternative approach to the accounting for, and reporting of, ND PP&E. This alternative approach is discussed below, with a detailed recommended revision of the ND PP&E definition and standard presented in Appendix A - *Recommended Definition and Standard*.

Recommended Approach and Basis for Conclusion

Recommendation

KPMG believes that the definition of, and the standard on, the accounting for, and reporting of, ND PP&E should be designed to provide optimal information for achieving the objectives of federal financial reporting and satisfying the information needs of users.

To this end, KPMG recommends that the definition of ND PP&E be modified to more closely reflect the operating environment of the DoD and to facilitate compliance with the recommended standard in Appendix A - *Recommended Definition and Standard*. Further, we recommend that certain PP&E currently classified as ND PP&E in SFFAS Number 11 be reclassified to appropriate non-ND PP&E categories, specifically, general PPP&E or operating materials and supplies. Examples include Weapons Systems Support Principal End Items, Weapons Systems

Support Real Property, and the missile component of Weapons Systems PP&E category, except for Intercontinental Ballistic Missiles and Submarine Launched Ballistic Missiles.

KPMG recommends that the standard on the accounting for, and reporting of, ND PP&E provide for the capitalization of ND PP&E program acquisition costs on the balance sheet. The conceptual basis for this recommendation is that ND PP&E represents an economic resource with future service potential.

With respect to the periodic measurement of cost and operating performance, given that ND PP&E Major End Items (e.g., aircraft, ships and combat vehicles) have an unpredictable life and are subject to premature obsolescence and are subjected to continual maintenance and repairs in order to maintain them in a constant state of readiness, it is appropriate to limit the measurement of operating costs to the costs of operations and maintenance, exclusive of depreciation. Depreciation accounting would not be required for Major End Items⁴ in as much as condition and readiness is not allowed to diminish for these items. With respect to other ND PP&E, categorized by KPMG as Other ND PP&E, costs should be allocated to benefiting periods because such ND PP&E generally have a more predictable life and are less susceptible to premature obsolescence. The standard should recognize the acceptability of accumulating costs in homogenous cost pools and composite cost allocation as an acceptable methodology for allocating the cost of Other ND PP&E to benefiting periods and programs.

In addition, the standard should include a requirement to disclose the quantity and report on the condition of ND PP&E Major End Items to provide information useful in assessing the effectiveness of the DoD's ND PP&E management of such items. However, the condition of Major End Items changes rapidly. Aircraft can change from Full-Mission Capable to Not Mission Capable and return to Full-Mission Capable in a matter of hours or days. Moreover, the criteria for determining condition is imprecise. For example, DoD Instruction 3110.5, the subject of which is "Material Condition Reporting for Mission-Essential Systems and Equipment," uses terms like "safe" as one of the criteria for determining Full-Mission Capable. Another criterion includes having all mission-essential subsystems installed and operating as designated by a Military Service. This could result in similar condition being assessed differently by the various Military Departments. Furthermore, as is the case with all DoD policy, the Military Departments issue more definitive guidance resulting in measurement variations between the services. This is a situation similar to that experienced by the FASAB in its discussion of deferred maintenance. Accordingly, KPMG recommends that the proposed condition information be defined as Required Supplementary Information (RSI) to provide for a period of experimentation with reporting alternatives to optimize the meaningfulness of the information. To address budgetary integrity, the standard should provide for disclosure of current year and cumulative cost information for major ND PP&E acquisition programs. This proposed requirement would provide readers with information on a defined number of individual major ND PP&E acquisition programs for use in comparisons with budgetary plans and limitations.

FASAB also should give careful consideration to two important issues, capitalization at transition and effective dates for implementing the standard.

⁴ *Major End Items are defined in Appendix A - Recommended Definition and Standard.*

With respect to the capitalization of ND PP&E at transition, KPMG recommends that the FASAB adopt a standard that limits the recognition to the cost of ND PP&E acquisition programs in the development or production phase and existing ND PP&E Major End Items. In addition, KPMG recommends that the FASAB provide an approach that minimizes the cost of valuation, given the complexity of the ND PP&E acquisition process, the budgetary focus of DoD's accounting processes, and the utility of such transitional information. Such a standard might recognize the acceptability of using Selected Acquisition Reports and other budgetary report information to value the acquisition program costs in the development and production phases and Major End Items at transition.

With respect to effective dates, KPMG recommends that the FASAB provide for phased implementation beginning with unit and condition reporting of Major End Items for the years ending after September 30, 2001 and the capitalization of those ND PP&E program acquisition costs incurred in years ending after September 30, 2005. Also, for the years ending after September 30, 2005, KPMG recommends the capitalization of estimated ND PP&E program acquisition costs associated with acquisition programs in the development or production phase and Major End Items still in existence on October 1, 2005. The reason for this lengthy and timed implementation is the need for the DoD to develop policies for accounting for ND PP&E in accordance with the proposed standard, modifying acquisition and procurement processes and procedures, developing and implementing a system for extracting the required data for capitalization of program acquisition costs, the development of training materials and providing training to personnel on the requirements of the standard and policies, and the modification of the Defense Federal Acquisition Regulation Supplement and contracts to provide for contractor reporting of certain cost information. Such modifications and changes to policies, regulations, processes, procedures, contracts, controls, and systems are extensive and involve the acquisition, procurement, logistics, and financial management communities of the Offices of the Secretary of Defense, Military Departments and Defense Agencies. KPMG discusses an approach and associated costs in Section VII - *Implementation Issues, Cost Estimates, and Timelines*.

Section V - Summary of the DoD's Accountability and Accounting Systems

Introduction

This section summarizes the capabilities of the major systems used by the Military Departments to track and report ND PP&E information. Appendix D - *DoD's Accountability and Accounting Systems*, contains a detailed analysis of the capabilities of these systems. The objective of this information is to provide readers of this report with an understanding of the capability of the DoD's systems to account for and report information required by existing and proposed ND PP&E accounting and reporting standards.

Accountability Systems

The Departments of the Army, Navy, and Air Force use accountability systems to track ND PP&E items, such as combat vehicles, ships, and aircraft and to maintain a record of critical information about these items. The Military Departments use multiple automated and manual systems for performing this accountability function. These systems range in complexity from relatively simple databases to complex systems. For the most part, these systems were not designed to serve as traditional property subsidiary systems to accounting systems and, consequently, do not interface with DoD accounting systems, which capture information for financial reporting. Further, most ND PP&E accountability systems have serious limitations with respect to the capability of capturing financial information. The following paragraphs summarize major ND PP&E accountability system capabilities for each Military Department.

Army

The U.S. Army Logistics Support Agency (LOGSA), a component of the U.S. Army Materiel Command, provides the Army with logistics management and equipment support. LOGSA is responsible for the worldwide management of Army assets, including ND PP&E. LOGSA uses multiple systems for asset management, including:

- The Continuing Balance System-Expanded (CBS-X) which provides worldwide visibility for major Army assets and selected secondary (component) items. CBS-X receives information from a variety of sources, principally, the Standard Property Book System – Redesigned, which is discussed below.
- The Standard Property Book System-Redesigned (SPBS-R) which is the primary system used by Army tactical units (combat, combat support, and combat service support) to requisition and account for ND PP&E and report on ND PP&E readiness.

LOGSA obtains the majority of the required data from tailored extracts from CBS-X for ND PP&E. CBS-X receives the majority of information for ND PP&E in the possession of units/end

users from the SPBS-R, and for ND PP&E not in the possession of units/end users (such as those assets in depots) from the Commodity Command Standard System.⁵

Navy

The Navy uses 19 different systems to track and manage ND PP&E, five of which provide the majority of information for financial statement reporting.

- The Aircraft Inventory and Readiness Reporting System (AIRRS) which is used to capture information on aircraft.
- The Naval Vessel Registry (NVR) and the Craft and Boat Support System (CBSS) which are used to capture information on ships and service craft and small boats, respectively.
- The Missile History and Status Report System and the Conventional Ammunition Information Management System (CAIMS) which are used to capture information on guided, self-propelled ordnance.

Air Force

The Air Force has three primary ND PP&E tracking and management systems.

- The Reliability and Maintainability System (REMIS), which is used to capture information on aircraft and intercontinental ballistic missiles.
- The Comprehensive Engine Management System (CEMS), which is used to capture information on aircraft engines.
- The Air Force Equipment Management System (AFEMS), which is used to capture information on selected ND PP&E items, such as: (1) guided missile system components, (2) specialized nuclear handling equipment, and (3) pressure controlling instruments. AFEMS also accounts for general PP&E.

Table V-1, depicts the capabilities of the foregoing systems.

⁵ The majority of Army ND PP&E is in the possession of units/end users.

Table V-1

System Name	Information Captured								
	Quantity		Cost						
	Units	Adds/ Deletes	Acquisition	Maintenance	Modifi- cations	Over- Haul	Depre- ciation	Salvage	Disposal
Army									
1. CBS – X	N*	N	N	N	N	N	N	N	N
2. SPBS-R	Y	Y	Y**	N	N	N	N	N	N
Navy									
3. AIRRS	Y	Y	N	N	N	N	N	N	N
4. NVR	Y	N	N	N	N	N	N	N	N
5. CBSS	Y	Y	Y	Y	Y	Y	N	N	N
6. Missile History and Status Report System	Y	N	N	N	N	N	N	N	N
7. CAIMS	Y	N	Y	N	N	N	N	N/A	N
Air Force									
8. REMIS	Y	Y	Y	N	N	N	N	N	N
9. CEMS	Y	Y	Y	N	N	N	N	N	N
10. AFEMS	Y	Y	Y	N	N	N	Y	N	Y

* CBS-X does not capture individual items, but totals by organization and by type of asset.

** SPBS-R has a cost field, however, it contains standard – not historical – cost.

As depicted in Table V-1, these systems can account for individual units of ND PP&E and most can provide quantity addition and deletion information. However, several systems do not have the capability to capture cost information.

Accounting Systems

The Military Departments' accounting systems track fund authority, commitments, obligations, and outlays. These systems track this activity generally by budget line item or budget procurement activity code. As described in KPMG's tutorial report on the acquisition process, budget line items and budget procurement activity codes generally equate to an ND PP&E acquisition program, system or ND PP&E component(s).

Transactions (commitments, obligations, and outlays) are recorded in these systems using a document number that includes an accounting classification code. Typical document types include, contracts, purchase and delivery orders, procurement and work directives, and military interdepartmental purchase requests, etc.

The principal accounting systems that capture ND PP&E budgetary execution information are:

- The Standard Operations and Maintenance Army Research and Development System (SOMARDS) used by the Army.
- The Standard Accounting and Reporting System (STARS) used by the Navy.
- The General Accounting and Finance System (GAFS) used by the Air Force.

Table V-2, depicts the accounting classification coding structure for the foregoing systems.

Table V-2

<i>Army</i>	<i>Navy</i>	<i>Air Force</i>
<i>SOMARDS</i>	<i>STARS</i>	<i>GAFS</i>
Fiscal Station Number	Authorization Accounting Activity	Accounting and Disbursing Station Number
Reimbursement Source Code	Reimbursement Source Code	Accounts Receivable Sales Code
Allotment Serial Number	Bureau Control Number	Allotment Serial Number
Basic Symbol	Basic Appropriation Symbol	Appropriation Symbol
		Budget Authority (Major Force Program)
		Budget Authorization Account Number
Army Management Structure Code		Budget Program Activity Code 1-2 Budget Program 3-6 Project Number
Country Code	Country Code	Country Code
Department	Department	Department
Element of Resource	Object Class Code	Element of Expense Investment Code
Special Operations Decision Package		Emergency and Special Program Code
Fiscal Year	Fiscal Year	Fiscal Year
Fund Code	Fund Code	Fund Code
		Major Force Program (Budget Authority)
		Material Program Code
		Material Program Code, Task or EEIC
Operating Agency	Bureau Control Number	Operating Agency Code
Allotment Serial Number	Bureau Control Number	Operating Budget Account Number
	Organization Code	Organization Code
Army Management Structure Code	Program Year	Program Element Code
	Army Management Structure Code	Program Year
Management Decision Package	Cost Account Code	Responsibility Center/Cost Code
		Sales Code
Standard Document Number	Standard Document Number	Standard Document Number
Limit	Subhead	Subhead

The Army, Navy, and Air Force use transaction code-based systems whereby transactions are posted in accordance with instructions associated with assigned codes. These systems currently capture commitments, obligations, and outlays associated with ND PP&E acquisition programs using the account structure described above. While the DoD does not currently capitalize the cost of ND PP&E acquisition programs, these systems are capable of accounting for capitalized costs. With respect to accounting for depreciation, each system has the capability to capture such information, but is dependent on other systems for the calculation of depreciation and the posting of depreciation requires manual intervention.

Section VI - Audit Issues

Introduction

The American Institute of Certified Public Accountants' *Codification of Statements on Auditing Standards* AU Section 326.02 states that:

Most of the independent auditor's work in forming his or her opinion on financial statements consists of obtaining and evaluating evidential matter concerning the assertions in such financial statements.

Assertions are representations by management, which are embodied in the various components of its financial statements (i.e., assets, liabilities, revenues, expenses, note disclosures, etc.). Management is responsible for complying with generally accepted accounting principles (GAAP) in the United States. Management usually accomplishes this by establishing policy. Management also develops and implements internal control systems to help ensure compliance with policy. Internal control systems help ensure that transactions and events are properly recorded, processed, summarized, and reported consistent with the assertions embodied in the financial statements. The following describes management's assertions that are embodied in its financial statements.

- Existence or occurrence – Assets and liabilities of the entity exist at a given date and recorded transactions occurred during a given period.
- Completeness – All transactions and accounts that should be presented in the financial statements are included.
- Rights and Obligations – Assets are the rights of the entity and liabilities are the obligations of the entity at a given date.
- Valuation or allocation – Asset, liability, equity, revenue, and expense components have been included in the financial statements at accurate amounts.
- Presentation and disclosure – Particular components of the financial statements are properly classified, described, and disclosed.

The following table correlates the provisions of the proposed ND PP&E accounting and reporting standard with the applicable assertions.

Table VI-1

<i>Accounting and Reporting Requirements</i>	<i>Financial Statement Assertions/Audit Objectives</i>				
	Existence or Occurrence	Completeness	Rights and Obligations	Valuation or Allocation	Presentation and Disclosure
Capitalize the cost of acquisition programs- disclose information about major acquisition programs	All reported transactions occurred during the year	All transactions that should be presented are included	ND PP&E acquired through acquisition programs are owned by the DoD	Program acquisition costs are reported at "full cost" as defined by federal accounting standards	Program acquisition costs are properly classified (i.e., reported in the proper programs) and disclosed
Capitalize the cost of existing ND PP&E	ND PP&E, which is represented by reported costs, exist as of the reporting date	ND PP&E acquisition programs in the development and production phases and Major End Items that should have been presented have been included	ND PP&E Major End Items reported in the financial statements are owned by the DoD	ND PP&E acquisition programs in the development and production phases and Major End Items are valued in accordance with federal accounting standards	ND PP&E valuation disclosures are in accordance with federal accounting standards
Disclose quantities of Major End Items	See Required Note Disclosures				
Write-offs upon obsolescence, destruction, disposition, or program termination	ND PP&E write offs are supported by evidence that the underlying event occurred	ND PP&E that should have been presented as written off have been reported as such	N/A	ND PP&E write offs were calculated in accordance with federal accounting standards	ND PP&E write offs have been appropriately disclosed in the Notes as a reduction in the value of ND PP&E programs
Allocation of the costs of Other Military Specific PP&E	N/A	Allocations of Other Defense Specific ND PP&E have been applied to all such PP&E	N/A	Allocations of Other Defense Specific PP&E are in accordance with federal accounting standards	The effects of allocating Other Defense Specific ND PP&E have been properly disclosed
Condition Assessment	See Required Note Disclosures				

<i>Accounting and Reporting Requirements- Required Note Disclosures</i>	Financial Statement Assertions/Audit Objectives				
	Existence or Occurrence	Completeness	Rights and Obligations	Valuation or Allocation	Presentation and Disclosure
Major End Items	All quantities of Major End Items disclosed in the Notes exist as of the reporting date	All quantities of Major End Items that exist as of the reporting date are disclosed	Major End Items disclosed are owned by the DoD	N/A	Major End Item quantities are properly classified by Major End Item type in the Notes
Condition Assessment Information	N/A	Condition assessment information pertains to all ND PP&E subject to the condition assessment requirement	N/A	Condition assessment information is based on standards, methodology, and rating scale established by management	Condition assessment standards, methodology, rating scale, and results have been disclosed in the Notes
ND PP&E Valuation Methods	N/A	N/A	N/A	N/A	ND PP&E valuation methods have been properly disclosed in the Notes
<i>Transition period disclosures</i>					
Program acquisition costs for the current and prior periods have not been included in the financial statements, and the future requirements for these costs	N/A	N/A	N/A	N/A	The Notes disclose that program acquisition costs for the current and prior periods have not been included in the financial statements, and the future requirements for these costs
Cumulative effect of adopting the revised ND PP&E standard	N/A	N/A	N/A	The amount of the cumulative effect was calculated in accordance with federal accounting standards	The Notes describe the nature of the restatement resulting from the adoption of the revised ND PP&E standard and its effect

Audit Issues

There is a direct relationship between the implementation issues, which we discuss in the next section, and the audit issues discussed below. Specifically, there are four major issues that affect the auditor's ability to obtain and evaluate evidential matter relating to the DoD's ND PP&E assertions and form an opinion on the DoD's financial statements. These issues are:

- Sufficiency of accounting policies for recording, processing, summarizing, and reporting ND PP&E transactions (as well as events and conditions) in accordance with federal accounting standards.

- Capability of information systems to record, process, summarize, and report ND PP&E transactions in accordance with the DoD's policies.
- Sufficiency of documentation to support the recorded ND PP&E transactions and events.
- Sufficiency of management's internal control program for monitoring compliance with accounting policies.

The following paragraphs provide a brief description of these issues.

Accounting Policies

Comprehensive accounting policies are the foundation for ensuring that the auditor can obtain and evaluate evidential matter relating to the DoD's assertions associated with ND PP&E. The DoD's existing ND PP&E policies provide for compliance with federal accounting standards but are not sufficiently comprehensive to ensure full and consistent compliance with the standards relating to ND PP&E.

The absence of comprehensive policies increases the risk of a material misstatement in management's assertions implicit in the financial statements. Stated differently, the absence of comprehensive policies increases the risk that the Military Departments will not record, process, summarize and report ND PP&E in accordance with federal accounting standards. The size and complexity of the ND PP&E activities would limit the auditor's ability to overcome this deficiency through extensive testing.

Information Systems

Effective information systems, which are a component of internal controls, are essential for ensuring that the Military Departments process, summarize, and report ND PP&E transactions and events promptly and accurately.

As described in Section V and Appendix D - *DoD's Accountability and Accounting Systems*, the DoD has numerous ND PP&E accountability and accounting systems, which, for the most part, have limited capabilities. As described in Section VII, the DoD's accounting systems have serious deficiencies, which inhibit the DoD from being able to improve the quality of financial information and comply with federal accounting standards.

The current state of the DoD systems will inhibit the auditor from being able to determine whether ND PP&E transactions are processed in accordance with the DoD's policies and federal accounting standards.

Documentation

Adequate documentation in support of ND PP&E transactions is critical to the audit process. Unless proper documentation to support recorded amounts is available, the auditor will not be able to form an opinion on the fair presentation of reported ND PP&E information. The DoD has experienced this problem in its efforts to obtain an opinion on the financial statements of

Other Defense Agencies. There are two components to the documentation issue: documentation requirements relating to ND PP&E valuation as of the date of transition to a revised standard, and documentation requirements for transactions and events that occur after the revised standard's effective date.

With respect to documentation in support of ND PP&E valuation as of the transition date, the sufficiency of evidence will be a function of the valuation criteria established in the revised standard. Given the complexity of the ND PP&E acquisition process and the principal objectives of capitalizing ND PP&E, it is critical that the FASAB establish practical criteria for arriving at the value of existing ND PP&E. Valuation criteria guidance is included in Appendix A – *Recommended Definition and Standard*.

The documentation requirements for transactions and events that occur after the effective date of the revised standard should be in accordance with accepted practice and be incorporated in the DoD's policies.

Internal Controls

Properly designed and functioning internal controls are the foundation for ensuring compliance with the DoD's accounting and financial reporting policies. Such internal controls reduce the risk of misstatements in ND PP&E financial information resulting from errors or irregularities.

Internal controls include five components: (1) the control environment, which sets the tone of the organization, and is the foundation for all other components of internal control; (2) risk assessment, which is the process used by an entity to identify, analyze, and manage risks relevant to the preparation of financial statements and related financial information; (3) control activities, which are the policies and procedures for ensuring that management directives are carried out; (4) information, which includes the accounting system and processes for ensuring transactions and related ND PP&E are properly recorded and reported, and communication, which involves providing an understanding of individual responsibilities for accounting and financial reporting; and (5) monitoring, which involves management's monitoring of internal controls to ensure they are operating as intended and that they are modified as appropriate for changing conditions.

The DoD must establish a properly functioning system of internal controls, which includes all of the foregoing components, to ensure the reliability of ND PP&E financial information. Given the magnitude of the ND PP&E acquisition process, a failure to establish appropriate internal controls will make an audit of ND PP&E financial information all but impossible.

Section VII – Implementation Issues, Cost Estimates, and Timelines

Introduction

To effectively implement the proposed ND PP&E standard, the DoD will need to accomplish the following:

- Evaluate and revise existing ND PP&E policies, regulations, and procedures at the DoD, Military Department, and Defense Agency levels.
- Evaluate and modify contracting practices for acquisition ND PP&E.
- Evaluate acquisition, procurement, logistics, and financial management systems and make modifications to or develop new systems for satisfying the ND PP&E accounting and reporting standard.
- Establish a comprehensive training program to include initial and recurring training for the acquisition, procurement, logistics, and financial management communities.
- Establish internal controls for ensuring compliance with policies and regulations.

KPMG recommends that the DoD consider establishing a joint management function responsible for ND PP&E accounting and financial reporting policies and implementation initiatives. The DoD's current organizational structure does not provide a corporate perspective with respect to the accounting for, and reporting of, ND PP&E. Rather, accounting policy flows from the Under Secretary of Defense (Comptroller) and operational policy emanates from other Under Secretaries and the Military Departments. Accordingly, effective implementation of the ND PP&E standard will require modifications to more than DoD accounting policies and accounting systems. Changes must also be made to DoD acquisition, procurement, and logistics policies and regulations, as well as systems. The recommended joint management function also must include oversight responsibilities over the acquisition, procurement, and logistics communities in order to effectively implement the requirements of the new ND PP&E standard.

Such a joint management function, comprised of the acquisition, procurement, logistics, and finance organizations, and led by the Office of the Under Secretary of Defense (Comptroller), would provide an effective communication link between the DoD Components and establish a mechanism through which the major ND PP&E stakeholders would be actively involved in the policy and systems requirements definition and implementation processes.

The following discussion addresses tasks that must be completed, whether through the current or a revised DoD structure, implementation timeframes and an estimate of the associated one-time costs. We did not address the on-going costs associated with implementation of the proposed standard inasmuch as the standard is designed to improve the quality of information used by the DoD's management, and, accordingly, we considered such costs to be a necessary part of normal operations.

Policy and Procedures

The first major task, and the most important, is evaluating and revising existing ND PP&E accounting and reporting policies and procedures. Effective resolution of all other implementation issues is dependent upon competent policies and procedures. This task involves two subtasks.

The first subtask is to review and evaluate the DoD's acquisition, procurement, logistics, and financial policies and procedures, including those issued by Military Departments and Defense Agencies that acquire, use, or support ND PP&E. These Defense Agencies include organizations such as the Ballistic Missile Defense Organization and the U.S. Special Operations Command. The policies and procedures of the Defense Finance and Accounting Service, Defense Contract Management Agency, and Defense Logistics Agency also must be evaluated, since they play important roles in the acquisition, modification, and support of ND PP&E. In addition, the contracting regulations contained in the Defense Federal Acquisition Regulations Supplement also must be reviewed and modified accordingly to ensure that future DoD contracts for ND PP&E acquisitions are written in a manner that supports the requirements for capturing appropriate ND PP&E data. We estimate that this subtask could be completed in approximately two years at an estimated cost of \$4 million.

The second subtask involves revising existing accounting and reporting policies. This subtask is made complex by the number of organizations and systems involved in ND PP&E acquisition, logistics, accounting, and reporting, as well as the coordination and review process necessary for the effective implementation of major policy changes. We estimate that this subtask can be accomplished in approximately twenty four months at an estimated cost of \$4.5 million.

Contracting Practices

The second task involves the modification of the DoD's contracting practices. The DoD will need to modify the form of contracts, and possibly the provisions of existing contracts, to provide pricing of components of ND PP&E acquisition programs. Given the volume of contracts and complexity of the contracting process, we are unable to estimate the cost of this change. We believe that it is reasonable to expect that the DoD will need the full implementation period to make these changes.

Systems Changes

The third major task involves identifying and implementing needed acquisition, procurement, accountability/logistics, and accounting systems changes. This task will be difficult, costly, and presents the greatest risk, but is critically important for successful implementation of the ND PP&E standard. To accomplish this task, we considered two possible approaches. Both approaches must be preceded by a requirements definition phase in which the informational requirements of the standard are defined and capability of systems to collect and exchange this information assessed.

The first alternative involves modifications of existing ND PP&E acquisition, procurement, accountability/logistics, and accounting systems. This alternative would be extremely complex

and challenging since the DoD, Military Departments, and Defense Agencies plan to modify or replace a number of their existing ND PP&E acquisition, procurement, accountability/logistics, and accounting systems. Those systems not scheduled for modification or replacement are extremely complex. Modifications to the existing systems could entail a significant investment of time measured in years at a cost that we were unable to estimate. In addition, this alternative would be high-risk because existing systems may not be modified successfully. Moreover, we question the efficacy of this alternative given existing systems shortcomings and the activities underway at the Defense Finance and Accounting Service (DFAS) to modernize the DoD's accounting and financial management systems, both of which are discussed below.

The DFAS recently issued a concepts of operations draft document entitled, *End-to-End Finance and Procurement Joint Concept of Operations*. This document described the present environment of the DoD's accounting and financial management systems that support the acquisition and contract/vendor payment functions as one that lacks shared business rules, standard edits, and does not share data. These systems do not manage information from a DoD corporate perspective. The draft document also describes the DoD's systems as being dependent on both hard-copy and faxed information, and requires both electronic and surface mailing of necessary information. Also, there are multiple inputs of the same data, multiple unique system interfaces, long delays in receiving data, mismatched information, multiple manual reconciliations, and no valid audit trails.

Furthermore, this document describes how the DoD plans to address existing systems' deficiencies by performing procurement and contract/vendor pay functions in an automated environment involving the implementation and use of a variety of new systems. These systems include the:

- *DFAS Corporate Database* – a centralized repository of data that facilitates the sharing of data among systems and functions; among applications; and among users within and outside DFAS.
- *DFAS Corporate Warehouse* – a central repository of uniform data for shared access that supports the DoD network. It will derive its data from the DFAS Corporate Database and pass this data to other systems or make the data available to support specific activities.
- *Defense Procurement Payment System* – a single contract and vendor payment system using standard, shareable data and in an electronic commerce environment.
- *Standard Procurement System* – a system that provides full acquisition support and interfaces through the use of standard electronic data interchange transactions with the DFAS Corporate Database and Defense Procurement Payment System.
- *Wide Area WorkFlow-Receipt and Acceptance* – a system that allows vendors to submit invoices and receiving reports electronically to the DoD and have them routed through a workflow system for inspection, acceptance, receiving, and payment.
- *Defense Standard Disbursing System* – a single standard DFAS automated information system for collecting, processing, recording, and reporting disbursement data.

The foregoing issues and systems plans reinforce our concerns about the risks and effectiveness of proceeding with the first alternative. Moreover, we have been advised that many DoD Components and organizations within Military Departments have not embraced the DFAS concept and are testing and deploying other new systems to address their individual needs, which further complicates matters.

The second alternative involves the development of a data warehouse application or applications by the Military Departments and Other Defense Agencies that would extract ND PP&E program acquisition cost and other information from existing systems to meet the reporting requirements of the standard proposed in this report. If existing systems do not collect the information required to support the standard, modifications to those systems would be required. The major tasks associated with the development of a data warehouse application include:

- Assess the capability of existing systems to collect, exchange, and report the information required by the standard.
- Modify existing systems and processes to capture the required information, where practicable.
- Determine how to obtain information that is not available in existing systems, as modified.
- Estimating the size of the data warehouse to facilitate the selection of the appropriate database software and related hardware.
- Developing appropriate system interfaces.

This alternative would be less complex, less costly, and more risk adverse. We estimate that it could be completed in a relatively short period of time, perhaps within three years, at a cost ranging from \$12-15 million. However, the cost-effectiveness of this alternative is questionable since the data would be derived from those systems and processes described in the DFAS concepts of operations document discussed above. While the majority of the data required for ND PP&E reporting under the standard proposed herein could be captured eventually, its quality would be questionable. We question the wisdom of spending millions to capture data of questionable reliability.

Accordingly, we recommend that the DoD immediately involve the acquisition, procurement, and financial communities responsible for ND PP&E accounting and reporting policies in the DFAS systems development initiatives. This involvement should include ensuring that systems' requirements address the accounting and reporting requirements of the final FASAB standard on ND PP&E. This would be the most cost-effective approach for addressing ND PP&E system shortcomings.

Concurrently, in recognition of the lengthy time required to complete major system initiatives, such as the DFAS initiatives, the DoD should assess the capability of existing systems and determine the minimal changes necessary for capturing the data required by the standard and the timeline required to complete the changes. If the projected timeline for completion of the DFAS

systems initiatives extends beyond the effective date of a final FASAB ND PP&E standard, the DoD may need to consider modifying existing systems and processes to capture required data. Once the DoD completes revisions to ND PP&E policies and procedures, modifications to existing systems, changes to business processes, and trains the Military Departments and Defense Agencies work force/personnel, which we discuss in the following paragraphs, the accounting infrastructure may be improved sufficiently to justify adoption of the data warehouse alternative.

Training

The third major task involves the development of a comprehensive training program and/or modifications to existing training programs and courses, which includes both initial and recurring training, for the new standard along with the DoD's revised policies and procedures. The DoD will need to review its entire training infrastructure to determine the changes needed to existing training programs and courses, such as those conducted by the Defense Acquisition University, Defense Systems Management College, National Defense University, and other formal Military Department training and educational organizations.

In addition to changes to existing training courses and programs, and due to the significant changes that will be required to implement the new standard, KPMG recommends that the initial training be classroom-based to facilitate an interactive learning environment. KPMG also recommends that the training be provided through a "top-down" approach, i.e., starting with senior executives and managers and then working down through the various levels to include those involved in the acquisition process, finance operations, and logistical functions. This classroom-based training program would involve many thousands of individuals and may require as long as two years to complete, once the training is developed.

The "top-down" approach will help to ensure support for the new standard at the highest levels of management. This "top-down" approach should provide for a tailored training program designed to meet the operational needs of specific groups.

The recurring portion of the training program should be two pronged – classroom training for new personnel and refresher or continuing training for those individuals that have already received classroom training. KPMG recommends that the refresher training be self-study, provided through a combination of web and personal computer-based applications.

We estimate that a comprehensive training program, which includes both the initial and refresher courses, could be developed within twelve to eighteen months at an estimated cost of \$5.0 to \$6.0 million. The cost of providing classroom instruction is dependent on the number of training sessions, which we believe should be provided at the base-level. We estimate the cost of base-level training at \$15,000 a session. The cost of refresher education is included in the development costs discussed above.

Summary

Due to the extensive changes and modifications that will need to be made by the DoD to policies, regulations, procedures, controls, and systems, KPMG recommends that the FASAB allow a

minimum of 5 years for full implementation of the ND PP&E standard. We estimate that the initial costs to fully implement the new ND PP&E standard, including the ultimate development of a data warehouse, exclusive of contract modification costs, could range from about \$25.5 to \$29.5 million. We expect the transition to the proposed standard would extend through the year 2004.

Appendix A - Recommended Definition and Standard

Recommended Definition of ND PP&E

1. National Defense, Property, Plant, and Equipment (ND PP&E) consist of PP&E essential to the performance of military missions by the Department of Defense. ND PP&E excludes PP&E accounted for in business operating activities, non-ballistic missiles, real property, and ND PP&E component parts held as spares.
2. Categories of ND PP&E include: (a) Major End Items⁶ and (b) Other ND PP&E. This categorization is intended to provide guidance in classifying ND PP&E.
 - a. *Major End Items:* Items that launch, release, carry, or fire a particular piece of ordnance and items that carry weapons systems-related property, equipment, materials, or personnel and have an indeterminate or unpredictable useful life due to the manner in which they are improved, modified, or maintained and because they are subject to premature destruction and obsolescence. (e.g., aircraft, ships, combat vehicles, etc.)
 - b. *Other ND PP&E:* All other ND PP&E items and Defense systems (e.g., National Missile Defense System, command and control systems, intelligence and communications systems, etc.), which are essential to the performance of military missions.

⁶ *End Item:* A final combination of end products, component parts, and/or materials that is ready for its intended use. (Definition from Joint Publication 1-02, "DoD Dictionary of Military and Associated Terms.")

Recommended Standard on Accounting for and Reporting of ND PP&E

Recognition and Measurement

Capitalization of Costs of ND PP&E Acquisition Programs⁷

1. The costs of acquisition programs related to the acquisition of ND PP&E, including the costs of acquisition programs that modify, modernize or otherwise improve existing ND PP&E, and the costs of ND PP&E acquired by means other than an acquisition program, should be capitalized as ND PP&E when incurred.⁸ Such costs should include the full cost of ND PP&E.
2. Costs of ND PP&E acquisition programs should be net of costs reimbursed or otherwise funded by other acquisition programs⁹ and funds provided to the DoD by foreign governments or international organizations for jointly developed or procured ND PP&E acquisition programs.

Establishing Capitalization at Transition

3. The initial capitalization amount for ND PP&E acquisition programs in the development or production phase and Major End Items in active service should be based on historical cost or latest acquisition cost. The initial capitalization amount for Major End Items should be the associated estimated acquisition program cost based on the number of Major End Items still in service as a percentage of the estimated number of Major End Items received under the program. If determining historical cost or latest acquisition cost is not practical because of inadequate records, estimated historical cost or latest acquisition cost may be used. Information acceptable for use in arriving at estimated historical cost or latest acquisition cost includes budget documents, appropriation documents, and other statutory or policy based reports reflecting amounts expended.

Alternatively, with respect to Major End Items, estimates of historical cost or latest acquisition cost may be derived by estimating the current replacement costs of similar Major End Items and deflating those costs to the acquisition year or estimated acquisition

⁷ An acquisition program is a directed, funded effort that is designed to provide new or improved ND PP&E in response to an operational need or to provide for the continued capability of existing ND PP&E.

⁸ This standard provides for the capitalization of the original investment in acquisition programs and modifications without adjustment for components replaced. Such components will be written-off in accordance with the provisions of paragraph 4.

⁹ This pertains generally to when an ND PP&E acquisition program acquires an ND PP&E component that is paid for initially by another ND PP&E acquisition program.

year if the acquisition year is unknown. Other approaches for estimating the acquisition costs of acquisition programs and Major End Items at transition may be utilized¹⁰.

Write-off Due to Obsolescence, Destruction, and Disposal

4. Major End Items may be decommissioned due to obsolescence, destroyed during conflicts and training, or otherwise taken out of service. Additionally, ND PP&E acquisition programs may be terminated prior to the delivery of planned Major End Items. The value associated with Major End Item decommissioning, destruction, or disposal, as well as terminated ND PP&E acquisition programs, should be expensed in the period such events occur.

Valuation of Obsolete, Destroyed, and Disposed Major End Items

5. The value of decommissioned, destroyed, or disposed Major End Items should be based on total associated capitalized ND PP&E acquisition program costs. The value should be based on a pro-rata share of the Major End Item's total associated capitalized ND PP&E acquisition program costs including ND PP&E acquisition program cost associated with modifications and improvements previously capitalized. In certain instances, Major End Items may be destroyed prior to full production and substantial ND PP&E acquisition program costs allocable to the entire estimated production run may have been incurred. When such an event occurs, the amount attributable to the destroyed Major End Item should be the item's pro rata share of estimated total ND PP&E acquisition program costs. The calculation of an item's pro rata share should be based on the total estimated acquisition program costs of the ND PP&E acquisition program and the estimated total number of Major End Items to be produced.

Expense Recognition

6. The value of obsolete, destroyed, and disposed Major End Items should be accounted for and reported as a reduction in the total capitalized costs of ND PP&E acquisition programs and as a loss from decommissioning, destruction, and program termination.¹¹

¹⁰ Capitalized ND PP&E acquisition programs consists of costs associated with the initial ND PP&E acquisition program and ND PP&E acquisition program costs associated with modifications and upgrades to the initially acquired ND PP&E. This standard recognizes the inherent imprecision that is expected to result from determining or estimating these costs for ND PP&E Major End Items acquired many years prior to the effective date of this standard in an environment in which the historical records were not required to be retained and may therefore be inadequate.

¹¹ Major End Items decommissioned and destroyed should be reflected as a deletion in the unit disclosure of changes in type or category of ND PPP&E.

Allocation of the Costs of Other ND PP&E

7. The cost of Other ND PP&E should be allocated to benefiting periods and programs in a systematic manner. A composite allocation methodology, whereby the costs of homogenous PP&E are allocated using the same allocation rate,¹² is permissible.

Condition Assessment

8. An assessment of condition, state of readiness, or mission capability¹³ is an important element in measuring the effectiveness of the management of ND PP&E. The condition of Major End Items should be assessed at a frequency interval deemed appropriate by management but not less than annually. It is desirable that condition assessments be based on generally accepted methods and standards. Condition assessments methods and standards should be consistently applied.

Required Note Disclosures/Required Supplementary Information

ND PP&E Acquisition Programs

9. The reporting entity should disclose current and cumulative activity in ND PP&E acquisition programs. The information disclosed should include:
 - a. Cumulative ND PP&E acquisition program costs at the beginning and end of the year for each major ND PP&E acquisition program.¹⁴
 - b. Current year capitalized ND PP&E acquisition program costs for each major ND PP&E acquisition program.
 - c. Planned or budgeted acquisition program costs for each major ND PP&E acquisition program.¹⁵
 - d. Reductions in capitalized ND PP&E acquisition program costs related to terminated ND PP&E acquisition programs for each active major ND PP&E acquisition program.

¹² The composite rate can be calculated based on a weighted or on an unweighted-average estimate of useful lives of assets in the composite.

¹³ Condition goals and assessments are required by Department of Defense Instruction Number 3110.5, *Material Condition Reporting for Mission-Essential Systems and Equipment*.

¹⁴ Major ND PP&E acquisition programs represent the 10 largest acquisition programs in planned dollar terms as designated by the Under Secretary of Defense for Acquisition, Technology, and Logistics.

¹⁵ Planned or budgeted acquisition cost information should be derived from the most recent *Selected Acquisition Reports (SAR)* or, for acquisition programs not subject to SAR reporting, amounts contained in the most recent *President's Budget*.

10. The disclosure also should include for each major ND PP&E acquisition program, the number of units¹⁶ originally projected for production under the acquisition program, the revised number of units projected for production,¹⁷ and the number of units delivered to date.

Major End Items

11. The reporting entity should disclose unit information by type or category for Major End Items.¹⁸ The information should include:
- a. Beginning and ending balances.
 - b. Additions and deletions during the period.

Other ND PP&E

12. The information disclosed for Other ND PP&E should include the following:
- i. The cost, associated depreciation, and net cost by major type, class, or composite group.
 - ii. The method(s) of depreciation for each major type, class, or composite group.
 - iii. The estimated useful lives of each major type, class, or composite group.

Condition Assessment Information

13. For each type or category of Major End Item, report as Required Supplementary Information (RSI) the following condition information.
- a. The condition assessment criteria.
 - b. The frequency of condition assessments.
 - c. Condition assessment for most recent three assessment periods.¹⁹

¹⁶ Units relate to types or categories of Major End Items, e.g., DDG-51. Unit reporting does not apply under this paragraph if the principal output of a major ND PP&E acquisition program is not measured in units, e.g., modifications to existing ND PP&E.

¹⁷ Projected unit information should be derived from the most recent SAR, or, for acquisition programs not subject to SAR reporting, most recent budget submissions.

¹⁸ Management should determine the types or categories to which this provision applies.

¹⁹ Trend information is not required for the year in which the standard is first effective. Two year trend data is required for the second year in which the standard is effective and three year data is required for the third year and all years thereafter.

ND PP&E Valuation Methods

14. The DoD should disclose the methods used for valuing ND PP&E acquired subsequent to the effective date of this standard and the methods for valuing ND PP&E acquired prior to the effective date of this standard.

Effective Date(s)

15. The requirements of this Statement are effective in two phases beginning with the fiscal year ending after September 30, 2001.

Phase one. For years ending after September 30, 2001 – the provisions requiring the reporting of units and condition assessment information for Major End Items apply.

Phase two. For years ending after September 30, 2005 – the provisions of this Standard apply prospectively to ND PP&E acquisition program costs incurred during years ending on and after the effective date.

Also for years ending after September 30, 2005 – the estimated acquisition program cost of ND PP&E acquisition programs in the development or production phase and Major End Items still in active service should be capitalized.

Required Note Disclosure During Transition Period

16. The reporting entity should disclose the reporting requirements for each of the transition periods, the fact that ND PP&E acquisition program costs for the current and prior periods have not been included in the financial statements, and the future requirements for these costs.
17. The cumulative effect of applying this standard should be reported as a restatement of beginning net position in the year applied. In the first year the standard is applied, the financial statements should disclose the nature of the restatement and its effect.

Illustrative Note Disclosures

The following sample footnote disclosures display the disclosure requirements of the proposed ND PP&E accounting standard. The amounts included are for illustrative purposes only and are not actual amounts or intended to be estimates of the actual amounts.

Adoption Disclosure

The following paragraph provides an example disclosure of the effect of adopting the standard.

Effective October 1, 2005, the DoD adopted Statement of Federal Financial Accounting Standard (SFFAS) No. X, “Accounting for National Defense Property, Plant and Equipment.” In accordance with SFFAS No. X, the DoD capitalized the estimated ND PP&E acquisition program costs relating to Major End Items in active service as of October 1, 2005 and the cost of acquisition programs in the development or production phase. The DoD restated its beginning net position to record the effect of this change in accounting principle as follows:

Balance Sheet Account	Balance Previously Reported on 9/30/2005	Adjustment	Restated Balance on 10/1/2005
ND PP&E	\$0	\$632,000	\$632,000
Net Position	(\$400,000)	\$632,000	\$232,000

Accounting Policy Disclosure

The following paragraphs illustrate disclosure of the accounting policy for ND PP&E.

The full cost of ND PP&E acquisition programs are capitalized when incurred, including the costs of ND PP&E acquisition programs that modify or upgrade existing ND PP&E. The full cost of ND PP&E acquisition programs are net of costs reimbursed or otherwise funded by other ND PP&E acquisition programs and funds provided to the DoD by foreign governments or international organizations for jointly developed or procured ND PP&E acquisition programs.

The costs capitalized as of October 1, 2005 include costs for major ND PP&E acquisition programs in the development or production phase and Major End Items in active service as of October 1, 2005. These costs were estimated based on an analysis of available program reports, such as budgets, budget execution reports, ACCT-RPT(M)1002 report, and Selected Acquisition Reports. In cases where such reports were not available, the capitalized costs were based on estimating the current replacement costs of similar Major End Items and deflating these costs through the use of price-level indexes to the known or estimated acquisition year.

The value associated with Major End Item decommissioning, destruction, or disposal and terminated ND PP&E acquisition programs are reported as a reduction in the total capitalized costs of ND PP&E acquisition programs and as a loss from decommissioning, destruction, and

program termination. The amount reported as a reduction/loss includes the Major End Item's pro-rata share of the total associated capitalized ND PP&E acquisition program cost.

The costs of Other ND PP&E are depreciated using the composite depreciation method. The composite depreciation rate is based on the following estimated average useful lives:

<u>Category</u>	<u>Estimated Average Useful Life</u>
Group 1	20 years
Group 2	15 years
Group 3	10 years
Group 4	5 years

Condition Assessment Policy Disclosure

The following illustrates footnote disclosure of the condition assessment criteria.

The DoD measures the condition status in accordance with DoD Instruction Number 3110.5, *Material Condition Reporting for Mission-Essential Systems and Equipment*. The DoD completes a condition assessment of ND PP&E at least once each year. The DoD reports the percent of ND PP&E that are Full-Mission Capable by major category or type of ND PP&E. Major End Items are considered Full-Mission Capable when they are safe and have all mission-essential subsystems installed and operating as designated by a Military Department.

ND PP&E Net Cost Disclosure

The following table illustrates footnote disclosure of the capitalized cost of ND PP&E less accumulated depreciation of Other ND PP&E.

The cumulative costs of Other ND PP&E is included in the cumulative cost of the ND PP&E acquisition programs. The cumulative costs of ND PP&E acquisition programs less the accumulated depreciation for Other ND PP&E is summarized in the following table.

(Amounts are in millions, are for illustration purposes only, and do not reflect actual results.)

Description	Balance 9/30/2006
Total ND PP&E Cumulative Cost	\$664,000
Less Accumulated Depreciation	(\$30,000)
ND PP&E Net	\$634,000

Other ND PP&E Cost and Accumulated Depreciation Disclosure

The following table illustrates footnote disclosure of the capitalized cost and accumulated depreciation requirements for Other ND PP&E.

(Amounts are in millions, are for illustration purposes only, and do not reflect actual results.)

Other ND PP&E	Cumulative Cost 9/30/2006	Accumulated Depreciation 9/30/2006	Net 9/30/2006
Group 1	\$28,000	(\$9,000)	\$19,000
Group 2	\$26,000	(\$8,000)	\$18,000
Group 3	\$24,000	(\$7,000)	\$17,000
Group 4	\$22,000	(\$6,000)	\$16,000
Total Other ND PP&E	\$100,000	(\$30,000)	\$70,000

Acquisition Program Cost and Units Disclosure

The following table illustrates disclosure of ND PP&E acquisition program information for each of the 10 largest programs (in monetary terms) designated as Major Acquisition Programs by the Under Secretary of Defense for Acquisition, Technology, and Logistics. The table also illustrates disclosure of the number of Major End Items originally projected for production, revised projected production, and delivered to date for each major acquisition program.

(Dollars are in millions and units are stated in number of Major End Items. Amounts are for illustration purposes only and do not reflect actual results.)

	ND PP&E Acquisition Program	Planned or Budgeted Cost	Cumulative Cost 10/1/2005	Current Year Capitalization	Current Year Program Terminations	Cumulative Cost 9/30/2006	Original Projection of Major End Items	Revised Projection of Major End Items 9/30/2006	Delivered Major End Items 9/30/2006
1	DDG 51 Destroyer	\$45,000	\$20,000	\$2,000	\$0	\$22,000	60	55	30
2	New Attack Submarine	\$28,000	\$17,000	\$2,000	\$0	\$19,000	20	20	10
3	C-17 Airlift Aircraft	\$25,000	\$15,000	\$2,500	\$0	\$17,500	80	75	50
4	F-22 Advanced Tactical Fighter	\$45,000	\$14,000	\$2,000	\$0	\$16,000	300	300	80
5	V-22 Osprey	\$28,000	\$12,000	\$2,500	\$0	\$14,500	120	120	60
...	Longbow Apache	\$24,000	\$9,000	\$500	\$0	\$9,500	100	80	70
10	Abrams Tank Upgrade	\$22,000	\$8,000	\$500	\$0	\$8,500	N/A- upgrade	N/A- upgrade	N/A- upgrade

Unit and Condition Assessment by Major Type/Category of ND PP&E

The following table demonstrates the reporting requirements for unit and condition information for Major End Items by major type or category. Disclosures include units at beginning of the year, units added, units deleted, and units at the end of the year information for the current year and the condition assessments for the past three periods. Condition information is defined as Required Supplementary Information.

(Units stated in number of Major End Items and percentages represent percent that is Full-Mission Capable.)

Type or Category	Beginning Balance 10/1/2005	Additions	Deletions	Ending Balance 9/30/2006	Condition Assessment Period 1	Condition Assessment Period 2	Condition Assessment Period 3
<i>Aircraft</i>							
Combat	8,660	52	351	8,361	79%	77%	75%
Airlift	6,059	23	148	5,934	94%	92%	90%
Other	3,740	67	247	3,560	76%	74%	72%
<i>Sub-total</i>	18,459	142	746	17,855			
<i>Ships</i>							
Submarines	123	1	7	117	68%	66%	64%
Aircraft carriers	18	0	0	18	67%	65%	63%
Surface Combatants	269	26	13	282	70%	68%	66%
Amphibious Warfare Ships	83	0	7	76	67%	65%	63%
Mine Warfare Ships	38	1	0	39	69%	77%	75%
Support Ships	241	6	33	214	72%	70%	68%
Other Ships	3,921	55	229	3,747	74%	72%	70%
<i>Sub-total</i>	4,693	89	289	4,493			
<i>Combat Vehicles</i>							
Tracked	44,522	328	684	44,166	85%	83%	81%
Wheeled	140,376	1,596	0	141,972	94%	92%	90%
Towed	7,044	0	78	6,966	78%	76%	74%
Other	12,744	829	19	13,554	79%	77%	75%
<i>Sub-total</i>	204,686	2,753	781	206,658			
<i>Ballistic Missiles</i>							
Ballistic Missiles	8,486	216	29	8,673	83%	81%	79%

Appendix B – Financial Reporting Objectives

FASAB Statement of Federal Financial Accounting Concepts (SFFAC) Number 1

SFFAC Number 1 includes four major categories of reporting objectives - budgetary integrity, operating performance, stewardship, and systems and controls. Each category has sub-categories that more fully describe the objective. The categories and related sub-categories follow.

Budgetary Integrity

Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised through taxes and other means and for their expenditure in accordance with the appropriations laws that establish the government's budget for a particular fiscal year and related laws and regulations. Specifically, federal financial reporting should provide information that helps the reader to determine:

- how budgetary resources have been obtained and used and whether their acquisition and use were in accordance with the legal authorization.
- the status of budgetary resources.
- how information on the use of budgetary resources relates to information on the costs of program operations and whether information on the status of budgetary resources is consistent with other accounting information on assets and liabilities.

Operating Performance

Federal financial reporting should assist report users in evaluating the service efforts, costs, and accomplishments of the reporting entity; the manner in which these efforts and accomplishments have been financed; and the management of the entity's assets and liabilities. Specifically, federal financial reporting should provide information that helps the reader to determine the:

- costs of providing specific programs and activities and the composition of, and changes in these costs.
- efforts and accomplishments associated with federal programs and the changes over time and in relation to costs.
- efficiency and effectiveness of the government's management of its assets and liabilities.

Stewardship

Federal financial reporting should assist report users in assessing the impact on the country of the government's operations and investments for the period and how, as a result, the government's and the nation's financial conditions have changed and may change in the future. Specifically, federal financial reporting should provide information that helps the reader to determine:

- whether the government's financial position improved or deteriorated over the period.
- whether future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due.
- whether government operations have contributed to the nation's current and future well being.

Systems And Control

Federal financial reporting should assist report users in understanding whether financial management systems and internal accounting and administrative controls are adequate to ensure that:

- transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and recorded in accordance with federal accounting standards.
- assets are properly safeguarded to deter fraud, waste, and abuse.
- performance measurement information is adequately supported.

FASB Concept Statement Number 1

The FASB's Concept Statement Number 1 relates to business enterprises. It establishes three broad reporting objectives for business enterprises. These objectives call for information that is useful in: (1) making investment and credit decisions, (2) assessing cash flows, and (3) understanding an enterprise's resources, claims to those resources, and changes in them. In order to meet these objectives, this concepts statement indicates that financial reporting should provide information:

- that is useful to present and potential investors and creditors as well as other users in making rational investment, credit, and similar decisions.
- to help present and potential investors and creditors as well as other users in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans.
- about the economic resources of an enterprise, the claims to those resources (obligations of the enterprise to transfer resources to other entities and owners'

equity), and the effects of transactions, events, and circumstances that change resources and claims to those resources.

- about an enterprise's economic resources, obligations, and owners' equity.
- about an enterprise's financial performance during a period.
- about how an enterprise obtains and spends cash, about its borrowing and repayment of borrowing, about its capital transactions, including cash dividends and other distributions of enterprise resources to owners, and about other factors that may affect an enterprise's liquidity or solvency.
- about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it.
- that is useful to managers and directors in making decisions in the interests of owners.

FASB Concept Statement Number 4

The FASB's Concept Statement Number 4 relates to non-business organizations. It establishes four broad objectives. These objectives call for information that is useful in: (1) making resource allocation decisions, (2) assessing services and ability to provide services, (3) assessing management stewardship and performance, and (4) understanding an organization's economic resources, obligations, net resources, and changes in them. This concepts statement indicates that financial reporting by non-business organizations should provide information:

- that is useful to present to potential resource providers and other users in making rational decisions about the allocation of resources to those organizations.
- to help present and potential resource providers and other users in assessing the services that a non-business organization provides and its ability to continue to provide those services.
- that is useful to present and potential resource providers and other users in assessing how managers of a non-business organization have discharged their stewardship responsibilities and about other aspects of their performance.
- about the economic resources, obligations, and net resources of an organization and the effects of transactions, events, and circumstances that change resources and interests in those resources.
- about an organization's economic resources, obligations, and net resources.
- about the performance of an organization during a period. Periodic measurement of the changes in the amount and nature of the net resources of a non-business organization and information about the service efforts and accomplishments of an

organization together represent the information most useful in assessing its performance.

- about the amounts and kinds of inflows and outflows of resources during a period.
- about the relation between inflows and outflows of resources during a period. Those who provide resources to a non-business organization and others want to know how and why net resources changed during a period.
- about the service efforts of a non-business organization.
- about the service accomplishments of a non-business organization.
- about how an organization obtains and spends cash or other liquid resources, about its borrowing and repayment of borrowing, and about other factors that may affect its liquidity.

An important point made by both of the foregoing FASB concepts statements is that financial reporting should include explanations and interpretations to help users understand financial information provided.

GASB Concept Statement Number 1

The GASB's Concept Statement Number 1 relates to operations of State and local governments. It establishes financial reporting objectives that apply to both governmental-type and business-type activities of State and local governments. The objectives and sub-objectives follow.

Financial reporting should assist in fulfilling government's duty to be publicly accountable and should enable users to assess that accountability by:

- providing information to determine whether current-year revenues were sufficient to pay for current-year services.
- demonstrating whether resources were obtained and used in accordance with the entity's legally adopted budget, and demonstrating compliance with other finance-related legal or contractual requirements.
- providing information to assist users in assessing the service efforts, costs, and accomplishments of the governmental entity.

Financial reporting should assist users in evaluating the operating results of the governmental entity for the year by providing information:

- about sources and uses of financial resources.
- about how it financed its activities and met its cash requirements.

- necessary to determine whether its financial position improved or deteriorated as a result of the year's operations.

Financial reporting should assist users in assessing the level of services that can be provided by the governmental entity and its ability to meet its obligations as they become due by:

- providing information about its financial position and condition.
- providing information about its physical and other nonfinancial resources having useful lives that extend beyond the current year, including information that can be used to assess the service potential of those resources.
- disclosing legal or contractual restrictions on resources and the risk of potential loss of resources.

Appendix C - Discussion of User Comments

Introduction

This appendix provides a detailed discussion of the results of KPMG's user survey. We present the results by survey subject and by user group. The survey included the following five topics:

- Capitalization of ND PP&E either on the balance sheet or as RSSI.
- Estimated loss in value of ND PP&E (Depreciation).
- Quantity and condition of ND PP&E.
- Actual versus planned ND PP&E investment information.

We also asked users about the importance of audited ND PP&E information. Our survey included four user groups: (1) citizens, (2) Congress, (3) executives, and (4) program managers. Our discussion begins by topic.

Capitalization of ND PP&E (Balance Sheet or RSSI) Summary

Eight respondents support reporting ND PP&E on the balance sheet. Reasons for supporting the balance sheet approach include the belief that ND PP&E is an economic resource by virtue of having future service potential and that this information would be assist in capital planning and demonstrating accountability. In addition, several respondents indicated that the total amount invested in ND PP&E is significant and therefore believe that the DoD's balance sheet is misleading without the ND PP&E. One respondent believes that ND PP&E is similar to general PP&E and, accordingly, should be reported in a like manner.

Six respondents do not believe that reporting ND PP&E on the balance sheet is useful. The respondents provided various reasons including ND PP&E represents a sunk cost; does not have a ready market and, accordingly, market value; and is not used as a basis for future decisions. One respondent stated the view that future spending is based on the defense capabilities of other countries, not on the monetary value of existing ND PP&E.

Estimated Loss in Value of ND PP&E (Depreciation) Summary

Six respondents stated the belief that depreciation is useful. The reasons for favoring depreciation included the belief that depreciation reflects consumption of the economic benefits or service potential of the assets; allows readers of financial statements to assess the condition of assets; provides a mechanism for charging the cost of capital to the respective users; and assists in calculating the expected annual costs of sustaining protective capability. One respondent also indicated that although defense spending fluctuates greatly each year, the actual costs incurred to operate the military are more consistent from year-to-year. Several respondents in favor of depreciation believe the depreciation method should be reasonable so that the accounting requirements are not burdensome to implement. One respondent expressed the view that certain

ND PP&E should not be depreciated, for example, ND PP&E that is preserved and maintained in a constant state of military readiness.

Eight respondents did not favor depreciation as they believe it is not used in determining whether to acquire new ND PP&E and that estimating the useful lives of ND PP&E is challenging. Several respondents indicated that the estimated useful life of ND PP&E changes frequently because the DoD continuously upgrades and refurbishes ND PP&E. Several respondents also expressed the view that depreciation does not apply to ND PP&E because the DoD maintains these assets in a constant state of military readiness, and, consequently, the costs for preserving and maintaining ND PP&E represents the true period costs.

Quantity and Condition of ND PP&E Summary

Eleven respondents believe that reporting quantity and condition information is useful. Several respondents believe that quantity and condition information demonstrates military readiness and other respondents believe the information illustrates accountability. Several respondents expressed the view that quantity and condition information assists management in the decision making process. However, some respondents also expressed concern about the affect of condition reporting on national security and others expressed concern about the cost of auditing condition information in relation to the benefits. One respondent recommended disclosing deferred maintenance related to ND PP&E and another respondent recommended disclosing the remaining useful life of ND PP&E.

Three respondents indicated that quantity and condition information does not belong in the financial statements; they believe accumulated depreciation reflects the effects of changing condition.

Actual versus Planned ND PP&E Investment Information Summary

Eleven respondents believe that actual versus planned investment information is useful. Some respondents expressed the view that this information would assist users in evaluating how well the DoD is managing its assets, particularly in terms of whether the Services obtained value for the costs incurred. One respondent believes that comparing the cost to maintain versus the cost to replace ND PP&E would be useful in future funding allocation decisions.

Three respondents did not view disclosing actual versus planned information as beneficial. One respondent argued that the costs of ND PP&E are sunk costs in economic terms and are not used to make future decisions. One respondent believes this level of detail of budget to actual information does not belong in the external financial statements. The respondent questioned the usefulness of planned versus actual information because the budget process is highly political and budgets are often adjusted to reflect changes in the original plan; therefore, the usefulness of this information to external users is questionable.

Importance of Audited ND PP&E Information

All fourteen respondents supported auditing ND PP&E information. The various reasons supporting audited information include the view that an audit provides assurances on the

accuracy of information, illustrates an organization's credibility, and drives improvement in the procedures and the internal controls.

Analysis of Comments by User Group

Capitalization of ND PP&E (Balance Sheet or RSSI)

Citizens

All four respondents supported reporting ND PP&E on the balance sheet. Several respondents believe that including ND PP&E on the balance sheet provides a more complete financial picture. One respondent indicated that reporting ND PP&E on the balance sheet allows the reader to assess the change in the DoD's financial position from period-to-period. Another respondent stated that ND PP&E have a future utility and therefore should be reported on the balance sheet. The respondent added by presenting ND PP&E on the balance sheet, users would be able to understand trends and changes in the DoD's assets.

One respondent believes that the United States Government should follow the proposed standard recently published for comment by the International Federation of Accountants, International Public Sector Accounting Standard Exposure Draft Number 14, *Property, Plant and Equipment*. This proposed standard specifically provides that military assets should be reported on the balance sheet at historical cost less accumulated depreciation because these assets meet the definition and the recognition criteria of PP&E, even though ND PP&E may have certain unique features. The proposed standard defines PP&E as:

...tangible assets that: (a) are held by an entity for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and (b) are expected to be used during more than one reporting period.

In addition, it provides that:

...property, plant and equipment should be recognized as an asset when: (a) it is probable that future economic benefits or service potential associated with the asset will flow to the entity; and (b) the cost or fair value of the asset to the entity can be measured reliably.

The respondent that advocated the use of international standards does not believe investment to date information is of value because it does not assist in making comparisons to other countries. The assumption being that other countries follow international accounting standards.

With respect to the level of information provided, one respondent whom supports reporting ND PP&E on the balance sheet believes that the DoD should report the total amount invested in ND PP&E by type and class of weapons system. This respondent added that reporting the total amount invested in a comparative format would enable users to determine the annual change in the investment.

One respondent does not believe that resources (i.e., time and effort) should be spent estimating the total amount invested for weapon systems that were acquired many years ago. Rather, the DoD should start tracking ND PP&E investments prospectively. Another respondent supports recording the cost of ND PP&E acquired to date and suggested that the DoD obtain reasonable estimates of the historical cost if the DoD is unable to determine the actual historical cost.

Congress

Two respondents believe that presenting ND PP&E on the balance sheet is useful. One respondent indicated that reporting the total amount invested in ND PP&E is part of the accountability process and that citizens have a right to information about the cost, quantity, and condition of weapons systems. This respondent added that ND PP&E information is important to appropriating the proper dollar amount for a given budget period.

One respondent believes that capitalization of the amount invested in ND PP&E may be useful, but feels that capitalization depends on the answer to the question: “to what end is the financial information being provided?” For example, while the General Accounting Office is interested in ensuring that agencies remain accountable, Congress may be most interested in the answer to questions such as, “why are the total costs or life-cycle costs of weapons systems increasing?” This respondent also believes that the capitalization process, if adopted by the FASAB, should only be prospective, because he respondent believes it is not possible (in reasonable terms) to estimate the acquisition costs for all existing weapons systems. As such, the format and level of detail in which information needs to be presented to demonstrate accountability versus that needed to provide information on cost trends may be significantly different.

With respect to implementing the balance sheet approach, this respondent also believes that the capitalization process, if adopted by the FASAB, should only be prospective, because the respondent believes it is not possible (in reasonable terms) to estimate the acquisition costs for all existing weapons systems.

The remaining two respondents stated that they do not see the value in presenting ND PP&E on the balance sheet and question the benefit of providing this information to Congress and the taxpayers. These respondents expressed the view that most ND PP&E does not have a market value since the DoD has no counterpart in the private sector. These respondents also expressed the view that cost information is not an appropriate measure of the utility or readiness of ND PP&E, and therefore, it does not provide users with information about whether the DoD’s mission is being achieved.

One respondent views the investment in ND PP&E as a sunk cost and believes the amount of funds invested in existing weapon systems is not used as a basis for future weapon systems spending decisions. Rather, this respondent believes future spending is based on the capabilities of the DoD relative to other countries. Also, this respondent believes that the time and effort of estimating the cost of existing ND PP&E would outweigh the value of the information to those who might use it.

Executives

The respondent believes that reporting the investment in ND PP&E on the balance sheet provides a complete picture of the government's economic resources. The respondent is also of the view that the capitalizing amounts invested in ND PP&E assists management with capital planning decisions (i.e., purchase, replacements, upgrades, and improvements) because the current remaining cost of weapon systems can be compared to prior periods and decisions on replacement versus upgrades can be made.

Program Managers

One DoD respondent believes that the Military Departments should report the aggregate value of ND PP&E because the Military Departments' investment in ND PP&E and the change in investment are important managerial indicators. This respondent also believes that the Services need to account for all their assets and value them at the proper cost. Most importantly, this respondent believes that the information underlying the financial statements (rather than the financial statements by themselves) is what is of greater importance because the underlying information is used to carry out certain managerial tasks, such as, monitoring projects-in-process and determining when to replace ND PP&E.

On the other hand, the other four DoD respondents indicated that the balance sheet perspective is not as important in the federal government as in the private sector because the risks are different. For example, management and users of private sector financial statements use asset information in the decision making process (implying investment and credit decisions). In contrast, DoD managers would not use ND PP&E balance sheet information to make investment decisions because future project costs and funding decisions are not based on the historical cost of weapon systems. These DoD respondents believe that capitalization should be limited to revenue producing enterprises because as the value of an asset decreases, the ability to generate revenue decreases. They also expressed the view that there is no ready market and, accordingly, no market value for ND PP&E.

What these four DoD respondents do believe is that the cost to maintain ND PP&E or acquire an alternative asset is relevant information. Specifically, program managers need to know the level of necessary maintenance, the approaches, the budget balances, and the residual impact.

Estimated Loss in Value of ND PP&E

Citizens

Three respondents believe that ND PP&E should be depreciated. One respondents believes that accumulated depreciation is an indicator of the condition of ND PP&E and precludes the need to report other condition information in the financial statements. This respondent added that the DoD should depreciate ND PP&E using a reasonable approach that is representative of the actual use and loss of asset value. Another respondent in favor of depreciation expressed the belief that depreciation accounting is only appropriate for ND PP&E that loses capability and not appropriate for ND PP&E that is maintained in a military state of readiness. This respondent stated that the cost of preserving and maintaining ND PP&E in a constant state of readiness is the

real period cost. The last respondent that favors depreciation stated that ND PP&E should be depreciated in accordance with proposed international standard for the public sector on accounting for property, plant and equipment. This proposed standard provides that:

The depreciable amount of an item of property, plant and equipment should be allocated on a systematic basis over its useful life. The depreciation method used should reflect the pattern in which the asset's economic benefits or service potential is consumed by the entity.

The one respondent who does not favor depreciation believes it is meaningless as depreciation represents the use of an asset, and the use of ND PP&E from period-to-period is difficult to estimate and quantify.

Congress

Two respondents indicated that depreciation information is useful. One respondent views depreciation as an interesting concept because it provides users a sense of the remaining life of an asset and an indication of the need to further invest in ND PP&E. This respondent also indicated that depreciation may provide valuable information for making investment decision in conflicting priorities; for example, in deciding whether to invest in new systems or to fund repairs, maintenance, and upgrades of existing systems. The other respondent believes that the depreciation process, if FASAB adopts a depreciation standard for ND PP&E, should only be prospective because the respondent believes it is not possible to estimate reasonably the depreciation for all existing weapons systems.

Two respondents stated that depreciation is not beneficial financial information. One respondent believes that depreciation may not be recorded properly because the age of many weapons systems is constantly extended by upgrades, which requires constant re-evaluation of useful lives. This respondent stated that the DoD has been focusing on maintaining and upgrading of current systems and not on the procurement of new weapons systems, which complicates the DoD's ability to accurately calculate useful lives. The respondent also stated the view that the depreciated value of ND PP&E is not an appropriate measure of the military value of the assets. The other respondent believes that depreciation is not beneficial because management or Congress does not use the information in determining whether to acquire new ND PP&E. This respondent added that ND PP&E procurement decisions are based on the need to remain militarily competitive.

Executives

The respondent expressed the view that financial reporting of ND PP&E should include depreciation to provide a mechanism for charging the cost of capital to the respective users. The respondent stated that the introduction of cost accounting, including a charge for depreciation, would provide a mechanism for improving the decision process related to acquiring and using of weapons systems for each responsibility area within the DoD. The respondent also believes that depreciation would assist in calculating the expected annual costs of sustaining protective capability. Although defense spending fluctuates greatly each year, this respondent believes the actual costs incurred to operate the military are more consistent from year to year. The

respondent suggested that the federal government needs a mechanism to measure the cost of readiness.

Program Managers

All five DoD respondents believe that calculating depreciation is not beneficial, given that ND PP&E is continually maintained and upgraded so that the systems will be ready for military operations at any time. They indicated that the useful life continually changes as weapons systems are retooled and refurbished. For example, because of upgrades, the B-52 now has an expected life of 100 years, much longer than its original estimate.

Moreover, the respondents believe that depreciation would not impact decisions to replace ND PP&E. They stated that ND PP&E is replaced when it no longer has value for the purpose intended or no longer contributes to military readiness.

Quantity and Condition of ND PP&E

Citizens

Two respondents believe that quantity and condition information may be useful. One respondent recommended that the DoD report quantity and condition information by major weapon system or type of ND PP&E. The other respondent indicated that investment information along with quantity information would enable users to distinguish between investments in newly acquired ND PP&E and investments in upgrades.

The remaining two respondents believe that quantity and condition information is meaningless and does not belong in the financial statements. They expressed the view that the effects of changing condition are reflected through annual depreciation expense and accumulation of depreciation.

Congress

All four respondents believe that reporting quantity and condition information in the financial statements is useful. Several respondents expressed the view that quantity and condition information assists management in the decision making process. One respondent expressed the belief that by reporting quantity and condition information, the DoD demonstrates its ability to account for its major weapon systems.

One respondent believes that reporting quantity, latest cost, and unit cost information would be useful to both internal and external users. However, since the acquisition cost of ND PP&E changes frequently due to modifications, the definition of cost reported in the financial statements would need to be determined. The respondent also stated that while condition information is useful, the respondent believes that deferred maintenance should be reported because the cost of maintenance is often greater than the initial investment. The respondent added that information on age, readiness, and spare parts availability would also be useful.

Executives

The executive respondent believes quantity and condition information is useful in assessing military readiness as long as the remaining useful life of ND PP&E is also known and disclosed. The respondent added that this information should be accompanied by the related total cost invested in ND PP&E in order to adequately assess how well the government adhered to planned or budgeted goals.

Program Managers

Four DoD respondents believe that reporting quantity and condition information is useful for assessing readiness. However, several respondents were concerned that disclosing condition information may compromise national security while other respondents were concerned about the cost/benefit of auditing condition information. One respondent expressed the view that information by asset class, including number of assets, will assist analysts in assessing military readiness.

The remaining DoD respondent believes that neither quantity nor condition information is useful. This respondent added that reporting deferred maintenance information is useful and that this information should be audited.

Actual versus Planned ND PP&E Investment Information

Citizens

Three respondents believe that actual versus planned information is useful because it enables financial statements users to determine how the DoD is doing in relation to plans. One respondent recommended disclosing the estimated costs that are not funded so users will know what additional funding is needed in order for the DoD to meet its objectives. Another respondent believes that comparing the cost to maintain ND PP&E versus the cost to replace ND PP&E would be useful because that information would aid managers and Congress in determining how to allocate future funding. The third respondent believes the costs alone are not very meaningful, because actual versus planned cost information cannot be used to measure accomplishment, as this is measured by the number of wars prevented, not outputs generated.

One respondent does not favor providing actual versus planned information in the financial statements. This respondent expressed the view that actual versus planned information is useful to the curious but is not the type of information that should be included in the financial statements. The respondent believes that the financial statements are not used for operational and managerial decisions. The purpose of external financial statements, the respondent argues, is to simply report whether the federal government is doing better or worse than the prior year.

Congress

Two respondents believe that actual versus planned information is important to determining whether programs deviate significantly from budgeted costs and anticipated outputs. One respondent added that planned versus actual cost is very useful during the development stages of ND PP&E, while another respondent acknowledged the DoD's contention that outputs are not

necessarily an appropriate performance measure as they do not address readiness, a subjective measure.

Another respondent in favor of disclosing actual versus planned information believes that the cumulative costs of the ten largest weapons systems, in terms of dollars spent or expected to be spent, along with planned versus actual outputs, should be reported in the financial statements. This information would assist users in assessing how well the DoD is managing its assets. This respondent suggested that this information be disclosed in a stewardship report.

One respondent does not believe that investment to date and planned versus actual costs/outputs provide substantial benefit to users of financial statements. This respondent believes that the costs expended for ND PP&E are sunk costs in economic terms. The respondent added that these costs are not used to make economic decisions for the program or in assessing the future plans for the assets. The respondent added that these costs are useful only in the evaluation the costs of similar programs in the future. The respondent expressed concern over the lack of visibility in the operations and maintenance area since these costs represent approximately one third of all DoD expenditures.

Executives

The respondent believes that actual versus planned information could be useful if it reflects the original budget against actual period financial information.

Program Managers

Four DoD respondents believe actual versus planned information is useful. One respondent expressed the view that actual versus planned information is important to assessing whether the Military Departments obtained value for the costs incurred (an asset management perspective). Another respondent indicated that actual versus planned information is especially important at the detailed program level for internal managerial purposes, however, the respondent does not believe this information would be beneficial in the aggregate (i.e., at the financial statement level) because of the causes for variances in program costs. This respondent indicated that large variances result from Congressional actions, Military Department policy changes, and program changes. As a result these variances are difficult to explain and the explanations would be of questionable benefit to financial statement users.

The other DoD respondent sees no value in presenting actual versus planned cost information for ND PP&E.

Importance of Audited ND PP&E Information

Citizens

All four respondents believe that auditing ND PP&E is important because it provides assurances about the accuracy of the balances and adequacy of internal controls. One respondent indicated that financial statement audits identify issues that need to be addressed, help develop new policy decisions and drive changes in behavior.

Another respondent believes that audited statements will become more important to external users as the United States gets more involved in global operations. However, this respondent does not share the view that audited financial statements are useful for internal planning and controlling of operations nor as a method of understanding whether financial management and internal controls are adequate.

Congress

All four respondents believe that the financial statement audit is important as it provides a measurement of the accuracy of reported information. One respondents added annual audits illustrate an organization's level of credibility. Another respondent expressed the view that annual audits lead to increased quality of information and relieves the organization of certain duties to analyze program costs. A third respondent added that Congress may have difficulty justifying additional funding if the DoD cannot produce audited financial information.

Executives

The respondent believes that an audit is beneficial if the proper objectives are established. The respondent added that an audit should aim to reduce fraud, waste, and abuse by reporting on the effectiveness of the entity's systems and controls.

Program Managers

All five DoD respondents believe that an annual audit is useful. The respondents provided various reasons including an audit provides assurances as to the quality/reliability of information reported; whether processes are functioning effectively; and as a basis for persuading others of the need for improved accountability and control.

Other Comments on ND PP&E

The following are additional respondent comments.

Congress

One respondent believes that reporting information on future threats facing the government compared with the investments in ND PP&E to counter these threats is useful. The respondent added that this will provide users with information about the quality of these investments. The respondent used as examples the costs incurred on the B-1 and B-2 programs. The respondent believes that if investment to date information were provided along with the threat that the B-1 and B-2 programs were designed to address, perhaps Congress and others would ask more questions about the logic of continuing to invest in these programs.

Another respondent believes that the actual versus estimated repair and maintenance costs and the actual versus estimated operating costs for ND PP&E should be reported.

Executives

The executive respondent suggested that FASAB adopt a long-term effective date for a balance sheet standard in order to give the DoD time to implement an effective versus watered-down standard.

Program Managers

Two DoD respondents believe that the Selected Acquisition Report (SAR) contains information needed for decision-making. One DoD respondents indicated that the focus should be on improving systems that produce the SAR information.

Appendix D – DoD’s Accountability and Accounting Systems

This section presents, for each of the Military Departments, the major systems currently used to track and report ND PP&E information; and identifies, for each of the systems, the function of the system, how it operates, the system’s capabilities and limitations, and the reports it issues. This information has been included in the report to provide an appreciation for the DoD’s capacity to implement, with existing systems, accounting standards related to ND PP&E.

In the Required Supplementary Stewardship section of its FY 1999 financial statements, the DoD reported quantity information for the following ND PP&E categories:

- Aircraft – Combat, Airlift, and Other
- Ships – Submarines, Aircraft Carriers, Surface Combatants, Amphibious Warfare Ships, Mine Warfare Ships, Support Ships, and Other Ships²⁰
- Combat Vehicles – Tracked, Wheeled, Towed, and Other
- Guided, Self-propelled Ordnance – Missiles and Torpedoes
- Space Systems – Satellites
- Weapon Systems Support Real Property – Active Ammunition Bunkers, Active Missile Silos, and Active Satellite Ground Stations

The DoD also reported its yearly investments (expenditures)²¹ during the year of \$36.2 billion associated with the above categories of ND PP&E. This schedule also included the DoD’s investments in Principal End Items and Support PP&E and Other and General Mission Support PP&E.

ND PP&E Accountability Systems

The Military Departments--the Army, the Navy, and the Air Force--use a number of automated and manual systems to account for ND PP&E. These systems range in complexity from relatively simple databases to extremely complex and sophisticated systems. For the most part, these systems were not designed to serve as traditional accounting systems and do not interface with either acquisition or general accounting systems. Also, several systems were not designed to capture and report cost information. Further, KPMG found that multiple organizations are involved in ND PP&E data collection, analysis, and reporting, thus further complicating the ND PP&E accounting process. The following paragraphs provide, by Military Department, a description of the systems used along with associated capabilities and limitations.

²⁰ DoD defined other ships as Service Craft, Landing Craft Air Cushion, and Small Boats.

²¹ DoD defined investments as the outlays (expenditures) from its Procurement appropriations.

Department of the Army

On its FY 1999 financial statements, the Army reported quantity information in the following five ND PP&E categories:

- Aircraft – Combat, Airlift & Other
- Ships – Other
- Combat Vehicles – Tracked, Wheeled, and Towed
- Guided Self-propelled Ordnance – Missiles
- Weapons Systems Support Real Property – Active Ammunition Bunkers, and Active Missile Silos

The Army reported that FY 1999 expenditures (investments) for ND PP&E totaled about \$7.1 billion. Of this amount, about \$3.8 billion or 54 percent related to three categories - Aircraft, Combat Vehicles, and Guided, Self-propelled Ordnance. Approximately \$1.6 of the \$3.8 billion related to Aircraft Support Principal End Items and Combat Vehicle Support Principal End Items. The balance of \$3.3 billion of expenditures related primarily to General Mission Support PP&E.

The U.S. Army Logistics Support Agency (LOGSA), a component of the U.S. Army Materiel Command, provides the Army with logistics management and equipment support. LOGSA is responsible for the management of Army assets, including ND PP&E, worldwide. LOGSA uses multiple systems for asset management.

Primary ND PP&E Accounting Systems

The Army's primary management information systems for ND PP&E are:

- The Continuing Balance System-Expanded (CBS-X), which provides worldwide visibility for major Army assets (i.e., aircraft, ships, and combat vehicles), and selected secondary (component) items. CBS-X receives information from a variety of sources.
- The Standard Property Book System-Redesigned (SPBS-R), which is the primary system that Army tactical units (combat, combat support and combat service support) use to requisition and account for ND PP&E and also report ND PP&E readiness.

LOGSA obtains the majority of the required data from tailored extracts from CBS-X for ND PP&E. CBS-X receives the majority of ND PP&E information for assets in the possession of units/end users from the SPBS-R; and for those assets not in the possession of units/end users (such as those assets in depots) from the Commodity Command Standard System.

LOGSA also obtains information on Missiles from the Worldwide Ammunition Retail System and the Commodity Command Standard System. The Army obtains information on Active

Ammunition Bunkers and Active Missile Silos from the Integrated Facilities Management System.

Our review focused on CBS-X as the primary source and SPBS-R as the feeder system for ND PP&E quantity information. The capabilities of these two systems to capture financial reporting information is depicted in Table D-1.

Table D-1

Information Captured									
System Name	Quantity		Cost						
	Units	Adds/ Deletes	Acquisition	Maintenance	Modifi- cations	Over- haul	Depre- ciation	Salvage	Disposal
1. CBS – X	N*	N	N	N	N	N	N	N	N
2. SPBS-R	Y	Y	Y**	N	N	N	N	N	N

* CBS-X does not capture individual items, but totals by organization and by type of asset.

** SPBS-R has a cost field, however, it contains standard – not historical – cost.

The Army did not design CBS-X and SPBS-R to be financial reporting systems nor do these systems interface with either acquisition or accounting systems. Accordingly, these systems do not perform all the functions required by the various approaches discussed in Section VI – *Financial Reporting Approaches, Recommendations, and Basis for Conclusion*. A discussion of each system follows.

Continuing Balance System – Expanded (CBS-X)

The DoD did not include CBS-X in its Financial Management Plan, dated September 1999.

Function. The Army uses CBS-X for processing requisitions, preparing budgets, redistributing assets, forecasting transportation and maintenance requirements, and performing readiness analysis. CBS-X provides the official worldwide on-hand balances for ND PP&E, selected secondary items,²² or repair parts defined as reportable items. Secondary items generally represent ND PP&E Principal Support End Items or Other Support Items. CBS-X is the primary source for reporting ND PP&E quantity information on the Army’s financial statements.

System Operation. CBS-X is an integral part of the Distribution Execution System, an application that integrates several legacy “stove-pipe” systems to facilitate the transfer of information between these systems. CBS-X is designed to capture asset quantity information reflected in unit-level accountability systems. CBS-X receives information from the following systems:

²² Secondary items are important components such as engines, transmission, etc.

- Standard Property Book System-Redesign
- Commodity Command Standard System
- Defense Property Accountability System
- Army Medical Department Property Accountability System
- Army Materiel Command Installation Support System
- Manual property books (non automated)

CBS-X captures the majority of its information from SPBS-R. CBS-X receives information from SPBS-R at least weekly and, if necessary, on a daily basis. The Distribution Execution System provides information on requirements/authorization levels, on-hand balances, and the status of requisitions.

Capabilities and Limitations. CBS-X was designed to capture the total quantities of assets on-hand and on order by type of asset, identified by a line item number,²³ and at the unit level (commonly referred to as unit identification code).

CBS-X was not designed to (1) track individual assets, (2) capture expenditure information, (3) assign costs at the time of asset delivery, (4) calculate or capture depreciation, (5) capture modification or overhaul costs, or (6) capture salvage value or disposal costs.

Reporting. CBS-X has limited reporting capabilities and only provides three reports to units. These reports reflect whether CBS-X accepted the transactions processed and the status of the transactions. These reports do not provide information for financial statement purposes. CBS-X has a query capability for determining quantities of equipment authorized, on-hand, and on order by type of equipment at the unit level. To satisfy financial statement reporting, LOGSA uses specially designed extracts to obtain ND PP&E quantity information from CBS-X.

Standard Property Book System-Redesigned (SPBS-R)

Since SPBS-R is the primary source of ND PP&E information contained in CBS-X, KPMG also evaluated its capabilities to provide financial reporting information for ND PP&E. The DoD identified SPBS-R as a critical Army property management feeder system in its Financial Management Plan, dated September 1999.

²³ The line item number is a six-character alphanumeric identification of ND PP&E and general PP&E listed in Army supply bulletins and equipment authorization documents. The line item number collectively treats all national stock numbers that possess the functional capability of the generic equipment. Line item numbers consist of one letter and five Arabic numerals and range from A00001 through Z99998. Line item numbers between A00001 and Y99989, except those starting with 0, are assigned to items included in chapters, 2, 6, or 8. Z series line item numbers are assigned to development type items for inclusion in required operational capability, and in authorization documents prior to type classification, and for use in special studies for development data required for type classification.

Function. SPBS-R is the primary property accountability systems for tactical Army units. SPBS-R provides the authorized property quantity level for a unit and processes order requisitions and requests to turn-in equipment. Further, SPBS-R serves as the source of quantity information for ND PP&E captured in CBS-X.

System Operation. SPBS-R is the primary data entry point for ND PP&E and provides information on ND PP&E balances and transactions to CBS-X.

The Army Authorization Document System is a system that the Army uses to determine personnel and equipment requirements along with how a particular unit should be organized. The Army Authorization Document System provides an extract that includes a unit's current and projected authorizations of equipment, including ND PP&E. LOGSA converts the data from the extract into an SPBS-R format and electronically distributes this information to update a unit's equipment authorization level, which is the basis for a unit to requisition or turn-in ND PP&E. Once a unit is authorized to have specific equipment, it submits a requisition for that equipment. Likewise, if a unit possesses equipment that it not authorized, the unit processes a request for turn-in. Upon receipt or turn-in of the equipment, the unit closes out the requisition and either increases or decreases the quantity of ND PP&E reported as on-hand in SPBS-R.

Capabilities and Limitations. SPBS-R was designed to (1) track individual asset quantities, (2) capture addition and deletion quantities, and (3) capture costs at the time of asset delivery.

SPBS-R was not designed to (1) retain historical cost data,²⁴ (2) calculate or capture depreciation, (3) capture modification or overhaul costs, or (4) capture salvage value or disposal costs.

Reporting. SPBS-R produces more than 50 different reports for various property management functions such as reports that reflect errors or discrepancies, a history of transactions, and equipment excesses. SPBS-R has the capability to produce two financial reports.

- The Capital Equipment Listing reflects assets, by type (line item) and funding source (Procurement, Operations and Maintenance, Army Stock Fund, and other funds). However, as previously discussed the cost field contains the standard cost of the asset as reflected in the Army Master Data File.
- The Standard Finance System General Ledger Report reflects summary-level dollar values. However, the Army does not use this report as it is based on standard cost information contained in the Army Master Data File.

²⁴ The cost field contained in SPBS-R is automatically updated to reflect an asset's standard cost.

Department of the Navy

On its FY 1999 financial statements, the Navy, including the U.S. Marine Corps, reported quantity information in the following six ND PP&E categories:

- Aircraft – Combat, Airlift, and Other
- Ships – Submarines, Aircraft Carriers, Surface Combatants, Amphibious Warfare, Mine Warfare, Support, Other, and Small Boats
- Combat Vehicles – Wheeled, Tracked, and Other
- Guided, Self-propelled Ordnance – Torpedoes and Missiles
- Space Systems – Satellites
- Weapon Systems Support Real Property

The Navy reported that FY 1999 expenditures for ND PP&E totaled about \$17.2 billion. Of this amount, the Navy reported that it expended about 71 percent or \$12.2 billion related to the three categories of Aircraft, Ships, and Guided, Self-propelled Ordnance. The Navy also reported it expended another 15 percent or \$2.5 billion on Aircraft and Ship Principal Support End Items and Other Support Items (such as aircraft engines) and 11 percent or \$1.9 billion on General Mission Support PP&E. The Navy reported the remainder in various categories such as Space Systems and Combat Vehicles (used by the U.S. Marine Corps).

Unlike the Army and Air Force, the Navy has multiple organizations that acquire and manage ND PP&E.

Primary ND PP&E Accounting Systems

The Navy has 16 different management information systems it uses to track, manage, and maintain ND PP&E.²⁵ Table D-2 identifies the 16 systems and provides a brief description.

²⁵ We did not attempt to determine the systems used to account for Marine Corps ND PP&E since it represents insignificant amounts - both in quantities and in expenditures - on the Navy's financial statements.

Table D-2

<i>System Name</i>	<i>Description</i>
1. Aircraft Inventory Readiness & Reporting System (AIRRS)	The Naval Air Systems Command (NAVAIR) operates AIRRS, which tracks all active aircraft by type, location, condition, and bureau number (each aircraft has a unique bureau number).
2. Naval Vessel Registry (NVR)	The Naval Sea Systems Command (NAVSEA) operates NVR, which tracks all Navy ships and service craft by individual item.
3. Craft and Boat Support System (CBSS)	NAVSEA operates CBSS, which tracks service craft and boats.
4. Conventional Ammunition Integrated Management System (CAIMS)	The Naval Supply Systems Command operates CAIMS, which is a classified system that tracks the location, quantity and condition for all non-nuclear, expendable ammunition.
5. Missile History and Status Report System	The Strategic Systems Program Office operates the Missile History and Status Report System which tracks the location and condition of Trident C-4 and D-5 ballistic missiles.
6. Satellite Tracking	Naval Space Command uses Satellite Tracking to track individual satellites.
7. Navy Facilities Assets Data Base (NFADB)	Naval Facilities Engineering Command (NAVFAC) uses NFADB to manage Navy owned and leased land, buildings, structures, and utilities.
8. Maximo Tracking Database	NAVAIR uses Maximo to track and manage inactive aircraft located at Davis-Monthan Air Force base.
9. Aircraft Engine Management System (AEMS)	NAVAIR uses AEMS to track all fleet-maintained Navy aircraft engines (engine propulsion system modules – EPSM) by type, location, condition, and serial number. Items in AEMS are considered ND PP&E support equipment end items.
10. Commercial Engine Tracking	NAVAIR uses Commercial Engine Tracking to track engines for 16 different support/commercial derivative aircraft programs such as the C-9, medium jet transport, and the C-130. Items are considered ND PP&E support end items.
11. Support Equipment Resources Management Information System (SERMIS)	NAVAIR uses SERMIS to track all Naval aviation support equipment by type, location, condition, and part number. Some, but not all, items are considered ND PP&E support items.
12. Calibration Standardization Asset Management System (CSAMS)	NAVAIR uses CSAMS to track all “out-of-service” calibration standards equipment by type, location, condition and serial number. Some, but not all, items are considered ND PP&E support items.
13. Metrology Automated System for Uniform Recall and Reporting (MEASURE)	NAVAIR uses MEASURE to track all “in-use” Navy calibration standards equipment by type, location, condition, and serial number. Some, but not all, items are considered ND PP&E support items.
14. Mobile Facility Automated Assets Control System (MFAACS)	NAVAIR uses MFAACS to track all mobile facility units, generators, frequency converters, power distribution boxes and mobilizers. Some, but not all, items are considered ND PP&E support items.
15. Financial Accounting & Inventory Record System (FAIRS)	The Naval Air Warfare Center operates FAIRS which tracks training systems/devices and training aid items.
16. Table of Organic Allowance Planning System (TOAPS)	Naval Special Warfare Command uses TOAPS to track all major special warfare and use equipment. Some, but not all, items are considered ND PP&E support items.

The Navy did not report any quantity information for Aircraft and Ship Principal Support End Items and Other Support Items or General Mission Support PP&E. Accordingly, we focused on

the five information systems that the Navy used to provide data related to the quantities reported for Ships, Aircraft, and Guided, Self-propelled Ordnance. The capabilities of these systems to capture financial reporting information is depicted in Table D-3.

Table D-3

<i>System Name</i>	Information Captured								
	Quantity		Cost						
	Units	Adds/ Deletes	Acquisition	Maintenance	Modifi- cations	Over- haul	Depre- ciation	Salvage	Disposal
1. Aircraft Inventory Readiness and Reporting System (AIRRS)	Y	Y	N	N	N	N	N	N	N
2. Naval Vessel Registry (NVR)	Y	N	N	N	N	N	N	N	N
3. Craft and Boat Support System (CBSS)*	Y	Y	Y	Y	Y	Y	N	N	N
4. Missile History and Status Report System	Y	N See Below	N	N	N	N	N	N	N
5. Conventional Ammunition Integrated Management System (CAIMS)	Y	N	Y Latest Acquisition	N	N	N	N	N/A	N

* CBSS and NVR both contain information on craft.

The Navy did not design these five systems to be financial reporting systems, nor do these systems interface with either acquisition or accounting systems. Accordingly, these systems do not perform all the functions required by the various approaches discussed in Section VI – *Financial Reporting Approaches, Recommendation, and Basis for Conclusion*. As reflected in the narrative part of the ND PP&E section of its FY 1999 financial statements, the Navy stated that:

...accountability and logistics systems do not contain a value for all or a portion of the ND PP&E assets. These systems were designed for purposes of maintaining accountability and other logistics requirements of ND PP&E, and not for reporting on the value of ND PP&E. Consequently, many of these systems do not accumulate costs or otherwise report values...

The following sections provide a detailed discussion of the five systems.

Aircraft

In the Aircraft category, the Navy reported quantity information in three subcategories—Combat, Airlift, and Other. The Navy obtained information regarding the quantities and types of aircraft from the Aircraft Inventory and Readiness Reporting System. The Navy also reported quantity information on inactive aircraft stored at the Aerospace Maintenance and Regeneration Center

(AMARC), located at Davis-Monthan Air Force Base. The Navy obtained this information from an Air Force system – the AMARC management information system.

Aircraft Inventory and Readiness Reporting System (AIRRS)

The DoD identified AIRRS as a critical Navy property management feeder system in its Financial Management Plan, dated September 1999.

Function. AIRRS provides near real-time information on Navy aircraft readiness, flight/utilization data and inventory status. It does so by tracking all Navy aircraft by type, location, and condition from initial delivery to disposal.

System Operation. AIRRS is a large-complex system that operates in a client-server environment, using a relational database. It uses 34 different files and interfaces with the Aircraft Engine Management System, the Support Equipment Resource Management Information System and several other systems. There are two primary sources of input – the Aircraft Custody/Status Change Report and the Aircraft Accounting Audit Reports.

The process of adding aircraft to the inventory, either from new production or by transfer from another Service, requires two steps. First, the aircraft must be assigned a unique bureau number. Second, an Aircraft Custody/Status Change Report must be submitted to indicate receipt of the aircraft with title to the Navy. Aircraft Custody/Status Change Reports are also sent whenever the custody, status or service life factor of an aircraft changes. Both items are transmitted in a message format.

Capabilities and Limitations. AIRRS is capable of capturing the following data:

- Controlling and Reporting Custodians
- Location & Status
- Operating Service Life
- Hours in Life
- Age Distribution

AIRSS was designed to predict an aircraft's retirement date which is calculated using an algorithm based upon factors such as operating service life, engineering service life, average utilization and other factors.

AIRRS was also designed to capture readiness data by individual aircraft at various organizational levels (i.e., squadron, wing, etc).

AIRRS was not designed to capture any cost information relating to acquisition, salvage value or disposal costs. Additionally, AIRRS was not designed to calculate depreciation.

Reporting. AIRRS has the capability to perform ad hoc queries using specific search criteria. AIRRS also produces various standard reports associated with status, readiness, and maintenance at various levels of detail down to each individual aircraft.

Ships

The Navy reported quantity information for eight different types of ships:

- Submarines
- Aircraft Carriers
- Surface Combatants
- Amphibious Warfare Ships
- Mine Warfare Ships
- Support Ships
- Other Ships
- Small Boats

Naval Sea Systems Command (NAVSEA) uses two systems – the Naval Vessel Registry (NVR) and the Craft and Boat Support System (CBSS) to capture quantity information regarding the different types for of ships. NVR is the primary system as the Navy only uses CBSS to obtain information for small boats.

Naval Vessel Registry (NVR)

The DoD identified NVR as a critical Navy property management feeder system in its Financial Management Plan, dated September 1999.

Function. The Navy uses NVR to capture specific information for its ships to meet various legal and other reporting requirements. NVR serves as the Navy’s official inventory system for ships and service craft and reflects the current status and assignment of ships and service craft.

System Operation. NVR, a standalone database system, does not interface with any other systems and relies strictly on manual data entry to update the database. The NAVSEA Shipbuilding Support Office is responsible for operating NVR and does so through an “informal” process. The office relies on information based on the receipt of various documents or telephone calls from at least eight different offices.

Capabilities and Limitations. The NVR database contains over 100 data elements. Thus NVR is capable of capturing a significant amount of information such as ship description acquisition-related data (i.e., builder and launch, delivery, and commission dates). NVR is also capable of capturing estimated useful life and the decommissioned date.

However, most NVR data elements are not financial-related. NVR was not designed to capture any cost information such as acquisition, salvage value or disposal costs. NVR also was not designed to calculate depreciation. NVR is not “transaction-based.” Thus it was not designed to report the number of ships added and deleted during a particular reporting period. However, information relating to changes in the status of ships are tracked in a remarks field in the database. Lastly, NVR was not designed to capture cost information related to ship overhaul and modifications.

Reporting. The Navy uses NVR to provide information on its ships to a variety of customers, including Congress. Prior to 1997, the Support Office distributed hard copy reports to over 400 customers. To reduce operating costs, the Navy created an NVR web site (www.nvr.navy.mil) to provide frequently requested information on Navy ships. Thus, the Support Office no longer produces periodic reports – instead it uses information from NVR to periodically update information on the web site. If the web site does not provide needed information, the Support Office queries the database to obtain the needed information. NAVSEA obtains ND PP&E information related to ships, including service craft, for the financial statements by having the Support Office query the NVR database and segmenting the ships by category (i.e., submarines, aircraft carriers, surface combatants, amphibious warfare ships, mine warfare ships, support ships, and other ships).

Craft and Boat Support System (CBSS)

CBSS contains information on service craft and boats. The DoD identified CBSS as a critical Navy property management feeder system in its Financial Management Plan, dated September 1999.

Function. The Navy uses CBSS to support life-cycle management of boats and service craft from initial delivery to disposal. In addition, it captures the condition, repair and maintenance costs and assists in the development, planning, programming and installation of alterations for service craft. NAVSEA obtains information relating to small boats from CBSS.

System Operation. CBSS, like NVR, is a standalone database that does not interface with any other systems. It relies strictly on manual data entry to update the database. NAVSEA's Program Executive Office, Expeditionary Warfare, operates CBSS on an "informal" basis. Official correspondence is the primary source of data.

Information relating to service craft is included in both NVR and CBSS. However, NAVSEA only uses CBSS to obtain information for boats. NAVSEA uses CBSS for life-cycle management of both service craft and boats.

Capabilities and Limitations. CBSS provides inventory management and control for both boats and service craft. CBSS was designed to capture a significant amount of financial-related information by individual service craft and boats, such as acquisition and disposal dates, acquisition documents (i.e., contract numbers starting in FY 1998), condition assessment, and repair, maintenance, and alteration costs. CBSS was also designed to capture cost information, however, the Navy does not record the acquisition cost in CBSS.

CBSS was not designed to capture salvage value or disposal costs, nor was it designed to calculate depreciation.

Reporting. CBSS has the capability to respond to ad hoc queries using specific search criteria. CBSS also produces various standard reports associated with alterations and contract management.

Guided, Self-propelled Ordnance

Within this category of ND PP&E, the Navy reported information in two subcategories – missiles and torpedoes.

Missile History and Status Report System

The DoD identified the Missile History Status and Report System as a critical Navy property management feeder system in its Financial Management Plan, dated September 1999.

Function. The Missile History and Status Report System tracks the location and condition of Trident C-4 and D-5 Fleet Ballistic Missiles.

System Operation. Navy missile information is extracted from two sources – Missile History and Status Report System and the Conventional Ammunition Integrated Management System (CAIMS). The Navy also uses CAIMS as the source of information for torpedoes. The Strategic Weapons Facility, Pacific located at Bangor, Washington uses an electronic spreadsheet to track the location and condition of individual Trident C-4 missiles. Data is entered manually, based on receipt of a DD Form 250, Material Inspection Receiving Report or a DD Form 1149 Requisition and Invoice/Shipping Document. There are no interfaces with any other systems.

The Strategic Weapons Facility, Atlantic, located at Kings Bay, Georgia uses a locally developed database to track the location and status of individual Trident D-5 missiles. Data is entered manually, based on receipt of a DD Form 250 or DD Form 1149. There are no interfaces with any other systems.

Capabilities and Limitations. The spreadsheet and database applications were designed to capture information on individual missiles, including the location and the condition (i.e., disassembled, expended, or disposed).

The spreadsheet and the database applications were not designed to capture financial reporting information such as acquisition, salvage value, or disposal costs. Also, the applications were not designed to calculate depreciation. Although the applications do not track additions and deletions, operating personnel have sufficient documentation to derive such information.

Reporting. Since the applications only involve a spreadsheet and personal computer-based database, information can be sorted and reported in any format.

Conventional Ammunition Integrated Management System (CAIMS)

The DoD identified CAIMS as a critical Navy property management feeder system in its Financial Management Plan, dated September 1999.

Function. The Naval Supply Systems Command uses CAIMS, a classified system, to track the location, quantity and condition of all non-nuclear expendable ordnance. Items include torpedoes, air-launched and surface-launched guided missiles, Tomahawk missiles, and all other conventional ordnance. Except for torpedoes and missiles, conventional ordnance does not meet the current definition of ND PP&E.

System Operation. CAIMS is a mainframe computer-based relational database. The Retail Ordnance Logistics Management System, used by field level organizations to track ordnance, is a primary feeder system.

CAIMS supports logistical management functions such as requirements determination, asset balances, requisition processing, tracking, cataloging, transporting and disposal. CAIMS provides information on both serviceable and unserviceable assets. Transaction Item and Ammunition Tracking Reports are the primary sources of data. Ammunition depots, weapon facilities, and other stockage activities submit these documents.

Capabilities and Limitations. CAIMS was designed to track individual assets by serial number. However, for some items, mainly conventional ordnance, CAIMS only tracks them by lot number. CAIMS was also designed to capture the acquisition cost along with additions and deletions. However, latest acquisition - not historical cost is recorded in CAIMS.

CAIMS was not designed to calculate depreciation or capture salvage value or disposal costs.

Reporting. CAIMS has an ad hoc query capability and produces a variety of reports.

Department of the Air Force

On its FY 1999 financial statements, the Air Force reported quantity information for the following four ND PP&E categories:

- Aircraft – Combat, Airlift, and Other
- Guided, Self-propelled Ordnance – Missiles²⁶
- Space Systems – Satellites
- Weapon Systems Support Real Property – Active Ammunition Bunkers, Active Missile Silos, and Active Satellite Ground Stations

The Air Force also reported quantity type information for some Principal Support End-Items and Other Support Items, such as uninstalled aircraft engines, avionics pods, and missile motors. In addition, it reported quantity information on inactive aircraft stored at the Aerospace Maintenance and Regeneration Center (AMARC), a subordinate organization of the Air Force Material Command, located at Davis-Monthan Air Force Base.

²⁶ *The Air Force identified two different types of missiles – intercontinental ballistic and tactical. Tactical missile quantities do not include those missiles that the Air Force considers to be classified.*

The Air Force reported that expenditures for ND PP&E totaled approximately \$10.9 billion. Of this amount, the Air Force reported that it expended about 90 percent or \$9.7 billion for Aircraft, Guided, Self-propelled Ordnance, and Space Systems with the remaining 10 percent or \$1.2 billion for Principal Support End-Items and Other Support Items.

Primary ND PP&E Systems

The Air Force's primary management information systems for ND PP&E are:

- Reliability and Maintainability System (REMIS) - REMIS captures and reports information on Aircraft and Intercontinental Ballistic Missiles.
- The Comprehensive Engine Management System (CEMS) – CEMS tracks aircraft engines and engine management information. CEMS interfaces with REMIS and exchanges data monthly.
- The Air Force Equipment Management System (AFEMS) – AFEMS accounts for both general PP&E and selected ND PP&E Support Principal End Items and Other Support Items, such as (1) guided missile system components, (2) specialized nuclear handling equipment, and (3) pressure controlling instruments.

The Air Force captures information on tactical missiles primarily in the Combat Ammunition System and the Department of the Army's Standard Depot System. The Air Force captures data on Weapons Systems Support Real Property in Air Force Civil Engineering System (ACES). These systems are not discussed in this report. Table D-4 summarizes the capabilities of REMIS, CEMS, and AFEMS.

Table D-4

<i>System Name</i>	<i>Information Captured</i>								
	Quantity		Cost						
	Units	Adds/ Deletes	Acquisition	Maintenance	Modifi- cations	Over- Haul	Depre- ciation	Salvage	Disposal
1. Reliability and Maintainability System (REMIS)	Y	Y	Y	N	N	N	N	N	N
2. Comprehensive Engine Management System (CEMS)	Y	Y	Y	N	N	N	N	N	N
3. Air Force Equipment Management System (AFEMS)	Y	Y	Y	N	N	N	Y	N	Y

The Air Force did not design these systems to be financial reporting systems. Except for CEMS, these systems do not interface with either acquisition or accounting systems. Accordingly, these systems do not perform all the functions required by the various approaches discussed in

Section IV – *Financial Reporting Approaches, Recommendation and Basis for Conclusion.* A discussion of each system follows.

Reliability and Maintainability System (REMIS)

The DoD identified REMIS as a critical Air Force property management feeder system in its Financial Management Plan, dated September 1999.

Function. Air Force system and item managers, logisticians, and engineers use REMIS to monitor the status and mission readiness of individual aircraft and associated weapon systems and components, such as engines, parts, automated test equipment, and communications equipment. These individuals also use REMIS to help determine reliability, as well as develop schedules for performing maintenance. REMIS provides “near real-time” inventory and maintenance data, which is accessible on-line. Other Air Force and DoD personnel also access and use REMIS. Air Force uses REMIS as the primary source for reporting quantities of ND PP&E in Air Force financial statements.

System Operation. REMIS is an on-line, transaction driven processing system that:

- Collects, processes, manipulates, stores, and retrieves data.
- Compares all incoming data to approved edit tables, possession records, configuration records, and other data.
- Provides interactive input and on-line viewing of data.
- Provides user activated queries and reports.
- Pushes edit tables to interfacing computer systems to ensure consistent use the same edit criteria.
- Collects and distributes data among selected base, depot, and HQ USAF level computer systems.

REMIS obtains information principally from the Core Automated Maintenance System (CAMS), which has two components - CAMS GO54 and CAMS GO81. CAMS GO54 is a standard Air Force information system that is used for ND PP&E tracking and management at the base level. CAMS GO81 performs the same functions as CAMS GO54 but is used exclusively by the Air Force Airlift Command. Data from CAMS GO54 is transmitted to REMIS about every hour. Currently, some CAMS GO81 data is transmitted daily while other data is transmitted monthly. CAMS GO81 data will be transmitted hourly beginning in October 2000.

Upon delivery of new aircraft and missiles, Aerospace Vehicle Distribution Officers enter the appropriate information in CAMS, such as date received, serial number(s), item description, assignment, and maintenance data. CAMS creates a Master Order Account and transmits the required information to REMIS.

Flight line crews provide maintenance data to base-level personnel who record it into CAMS. Generally, data entered include a narrative description of the maintenance, repair, or modification, including serial number information.

REMIS has three subsystems:

- Equipment Inventory, Multiple Status, Utilization Reporting Subsystem (EIMSURS)
- Product Performance Subsystem (PPS)
- Generic Configuration Status Accounting Subsystem (GCSAS)

Equipment Inventory, Multiple Status, Utilization Reporting Subsystem (EIMSURS)

The primary function of EIMSURS is to track and report ND PP&E levels (i.e., units), status (i.e., combat readiness), and utilization data (i.e., flying hours, landings, flights). EIMSURS maintains information at the end-item level, by item serial number. EIMSURS also maintains historical data on ND PP&E inventory gains, terminations, and status.

EIMSURS contains two sub functions – status and utilization.

The status sub-function provides information on the combat readiness of ND PP&E. For example, it produces mission-capable rating information. This information can be produced by equipment type and/or organization.

The utilization sub-function provides statistics for flying hours, landings, flights, etc, for aircraft and usage data on trainers and automated test equipment. It provides airframe hours and flying hours for each aircraft. The Air Staff uses this to determine flying hour allocations and help prepare the related portions of the Air Force budget.

Product Performance Subsystem (PPS)

PPS collects and provides maintenance information and information about manpower utilization per flight or flying hour. This information is used for conducting a full reliability and maintenance analysis of specific equipment items or groups. For example, analysts can use this data to identify negative trends relative to a particular ND PP&E component.

Generic Configuration Status Accounting Subsystem (GCSAS)

The GCSAS captures approved weapon system configurations, actual configuration status, and scheduled maintenance information. Base level and depot level personnel have “read only” access to approved configuration information. Actual equipment configuration data are submitted to REMIS as component removal and installation actions occur.

Capabilities and Limitations. REMIS was designed to capture the quantities of aircraft and missiles including selected individual installed components. REMIS identifies each aircraft by tail number and each missile and selected individual installed component by serial number. REMIS can report this data by assigned command and organization, program element, possessing command and organization, and Mission Design Series codes. REMIS was also designed to capture the acquisition cost of individual aircraft and intercontinental ballistic missiles, along with non-cost information on modifications, improvements, and repairs of aircraft and missiles, including exchanges of any serially numbered components. However, cost information is not consistently recorded.

REMIS was not designed to capture salvage value or disposal costs. REMIS was also not designed to calculate depreciation. REMIS does not capture all ND PP&E component parts as Air Force policy only requires recording those items having serial numbers.

The Air Force records ND PP&E components in storage or at depots in a separate accountability system - the Stock Control System, which is a supply and ordering system. This system performs the functions of processing requisitions, providing status of requisitions, maintaining visibility of assets (by quantity, condition, and location), and allocating and issuing assets for both the Air Force and the Marine Corps.

Reporting. REMIS provides on-line standardized inventory status and utilization reports. REMIS also has an on-line query and report capability that permits users to view all modifications, improvements, and repairs. REMIS can summarize and report ND PP&E information by type and category of asset, such as F-15 aircraft or combat aircraft.

Information included on reports for financial statement purposes consists of the following:

- Equipment designator (F-15A, F-15B)
- Block number (All F-15's)
- Beginning balance
- Unit cost of beginning balance
- Added (Number of units added)
- Unit cost of added units
- Deleted (Number of units deleted)
- Unit cost of deleted units
- Ending balance (In units)
- Unit cost of total ending balance

As previously discussed, the Air Force does not consistently record cost data, and it does not reflect the costs of modifications or improvements.

Comprehensive Engine Management System (CEMS)

The DoD identified CEMS as a critical Air Force property management feeder system in its Financial Management Plan, dated September 1999.

Function. The Air Force uses CEMS to track, manage, and maintain aircraft engines, which are Aircraft Support Principal End Items. CEMS interfaces with REMIS on a monthly basis.

System Operation. CEMS is a mainframe application and is comprised of seven subsystems:

- The Status Reporting and File Maintenance subsystem maintains central data and serial number information, supports central database inquiries, maintains a record of assets, supports engine parameter estimates, and provides data for determining reliability and maintainability policy/procedures.

- The Inventory Management and Distribution subsystems use stock levels at Air Force bases to allocate and distribute engines.
- The Standards and Pipeline subsystem provides technical information.
- The Configuration Management subsystem uses inventory levels and remaining life to assist in forecasting requirements.
- The Time Compliance Technical Order Management subsystem tracks compliance with technical orders, reports technical order configuration, updates the technical order history, and determines tool requirements to comply with technical orders.
- The Actuarial subsystem provides exposure rates, reports removals and losses, provides engine installation reports and provides failure rates.

Capabilities and Limitations. CEMS was designed to capture individual items (by serial numbers) and additions and deletions. Also, CEMS has a cost field.

CEMS was not designed to capture salvage value, or disposal costs. CEMS also was not designed to calculate depreciation.

Reporting. CEMS is capable of providing status information along with maintenance and technical information.

Air Force Equipment Management System (AFEMS)

The DoD identified AFEMS as a critical Air Force property management feeder system in its Financial Management Plan, dated September 1999.

Function. Air Force uses AFEMS to manage general PP&E and certain items of ND PP&E. AFEMS identifies the authorization levels that permit Air Force units to acquire PP&E, accounts for PP&E, and reports on types and quantities of PP&E. For ND PP&E, AFEMS performs these functions for Support Principal End Items and Other Support Items, such as guided missile system components, specialized nuclear handling equipment, and pressure controlling instruments.

System Operation. AFEMS is a transaction-driven, relational database system. It obtains information from the Standard Base Supply System (SBSS), which captures data on (1) PP&E in the custody of user organizations, (2) PP&E that is in transit, (3) PP&E in a maintenance/repair status, and (4) PP&E in warehouses awaiting distribution. The Standard Base Supply System also captures data on operating materials and supplies. Upon receipt of ND PP&E, the receiving office submits receiving information to equipment management personnel who enter the required information into SBSS.

Cost information is obtained from applicable acquisition documents, such as a contract or purchase order, or vendor invoice.

Capabilities and Limitations. AFEMS was designed to capture (1) individual assets by serial number, (2) asset location (i.e., end user location, maintenance depot, etc.) (3) acquisition cost, and (4) asset additions and deletions. AFEMS also was designed to calculate depreciation, and capture salvage value, in addition to capturing information on proceeds received from asset disposal, and calculate the gain/loss upon asset disposition.

AFEMS was not designed to capture maintenance history and costs.

Reporting. AFEMS has the capability to report ND PP&E items and cost by type and class.

Accountability System Summary

The Military Departments use a variety of systems to account for ND PP&E. These systems were designed primarily for maintenance, readiness reporting and management purposes. Accordingly, these systems do not contain all the required data for ND PP&E financial reporting, as discussed in the DoD's Financial Management Plan, dated September 1999.

Accounting Systems

The DoD's regulations²⁷ require the Military Departments to report the annual procurement outlays for all ND PP&E assets using the DoD Components' budget execution 1002 Report, *Appropriation Status by Fiscal Year Program and Subaccounts*. However, for all three Military Departments, the accounting systems that provide data for the 1002 Report were designed primarily as budgetary execution systems. In their narrative statements on ND PP&E, all three Military Departments reported that:

The ND PP&E cost information is captured in the DoD accounting systems and reported in the Department's "Statement of Net Cost." However, the Department's accounting systems were designed to provide appropriated fund accounting reports required by Congress, the Department and other applicable federal agencies. In addition, the accounting systems were not designed to accumulate and retain costs for individual items of ND PP&E.

These systems track funds authorized, obligated and disbursed – generally by budget line items. As described in KPMG's tutorial report on the acquisition process, budget line items generally equate to an ND PP&E acquisition program, system or ND PP&E component(s).

The DoD Comptroller transfers appropriated funds to the Military Departments through the Program and Budget Allocation System by budget line item. Upon receipt of these funds the Military Departments, in turn, distribute the funds to subordinate commands. The subordinate commands then enter the fund authority into their respective accounting system. The Military Departments use these accounting systems, which were designed as budgetary execution systems, to track fund authority, commitments, obligations, and disbursements. These systems are the primary source of information for data contained in the budget execution 1002 Report.

²⁷ DoD Financial Management Regulation, Volume 6B, Chapter 11, paragraph 110203.

The following sections describe the operation of the respective Military Department systems and associated financial reporting capabilities.

Department of the Army

In its FY 1999 financial statements, the Army reported in the narrative statement on yearly investments for ND PP&E that:

Investment values included in this report are based on outlays (expenditures). Outlays are used instead of acquisition costs, because current DoD systems are unable to capture and summarize Procurement Appropriation acquisition costs in accordance with accounting standards.

Procurement Appropriations fund the acquisition of Army ND PP&E. For the Army, there were seven different Procurement Appropriations in the FY 2000 budget.

- Aircraft
- Missiles
- Ammunition
- Weapons and Tracked Combat Vehicles
- Other Procurement, Army – Activity 1
- Other Procurement, Army – Activity 2
- Other Procurement, Army – Activity 3

Within these seven appropriations, there are individual budget line items, which are grouped by activity codes. For example, funds for the Abrams tank program are appropriated in the Weapons and Tracked Combat Vehicles appropriation. In the FY 2000 budget, there were 45 budget line items²⁸ in this appropriation with the first 26 in activity code 1 – Tracked Combat Vehicles and the remaining 19 items in activity code 2 – Weapons and Other Combat Vehicles. The FY 2000 budget contained five budget line items for the Abrams tank:

Line Item 1 – Abrams Training Device Modernization
Line Item 9 – Abrams Tank Training Devices
Line Item 21 – M1 Abrams Tank - Modernization
Line Item 22 – Abrams Upgrade Program
Line Item 23 – Abrams Upgrade Program -Advanced Procurement

All five budget line items for the Abrams tank are listed under activity code 1 - the first two are listed under the heading of Tracked Combat Vehicles and the last three are listed under the heading of Modifications of Tracked Combat Vehicles. In addition, budget line item 45 – Spares and Repair Parts (Weapons and Tracked Combat Vehicles) contains funds for four programs - the Abrams Tank, the Bradley Fighting Vehicle, the Command and Control Vehicle, and the Heavy Assault Bridge.

²⁸ Budget line item numbers vary from year-to-year.

Primary System. The Army Materiel Command is the major command responsible for the acquisition of the majority of the Army's ND PP&E. It uses the Standard Operations and Maintenance Army Research and Development System (SOMARDS) for budgeting, accounting, and reporting for all appropriations other than working capital funds. SOMARDS was designed as a budget execution system.

System Operation. The Defense Finance and Accounting Service – Indianapolis operates SOMARDS, which is a mainframe computer database system. The Program Manager, Abrams Tank Systems receives funds from the Army Comptroller through the Program and Budget Allocation System by budget line item. Authorized funds are entered into SOMARDS using an eight digit Army Management Structure Code (AMSCO). The following chart reflects the definition of each position of the code:

<u>Position</u>	<u>Definition</u>
1	Appropriation
2	Budget Activity
3	Budget Subactivity
4	Budget Subactivity
5	DoD Sequence Number
6	DoD Sequence Number
7	DoD Sequence Number
8	DoD Sequence Number

AMSCOs relate directly to budget line items. For example, the Army Management Structure Codes for the Abrams Tank program are as follows:

<u>AMSCO</u>	<u>Line Item</u>	<u>Description</u>
31100330	1	Abrams Training Device Modernization
31106984	9	Abrams Tank Training Devices
31206406	21	M1 Abrams Tank - Modernization
31206500	22	Abrams Upgrade Program
31206501	23	Abrams Upgrade Program -Advanced Procurement
33104540	45	Spares & Repair Parts (Weapons & Tracked Combat Vehicles)

The program manager generally suballocates the authorized funds and within the suballocations, the program manager creates individual job orders to control the various aspects of its operations. The job order represents the lowest level of fund control.

Transactions (commitments, obligations, and disbursements) are recorded in the system using a document number that includes an accounting classification code. Typical document types include, contracts, purchase/delivery orders, procurement/work directives, travel orders, military interdepartmental purchase requests etc. SOMARDS interfaces with at least 11 other systems such as procurement, payroll, and supply. The structure of the Army accounting classification code is reflected in Table D-5.

Table D-5

ACCOUNTING CLASSIFICATION CODE		
U.S. Army Appropriation - Direct Funds 21 0 2020 57-3106 325796.BD 26FB QSUP CA200 GRE12340109003 AB22AB WORNAA S34031		
Code	Data Element	Explanation
	Treasury Symbol:	
21	Department Code	Department of Army
0	Period of Availability (FY)	Fiscal Year 2000
2020	Basic Symbol	Operations and Maintenance, Army
57	Operating Agency	U.S. Army Training and Doctrine Command (TRADOC)
3106	Allotment Serial Number	Locally Assigned
325796.BD	Army Management Structure Code	Base Operations (BASOPS-), TRADOC Director for Logistics (DOL)
26FB	Element of Resource	Supplies-Army Managed/DWCF Item
QSUP	MDEP/SODEP	Installation Supply Operations
CA200	Functional Cost Account	Commercial Activities - Contract Furnished Supplies
GRE12340109003	Standard Document Number	See Table 5-4
AB22AB	Account Processing Code (APC) and DPI Code or JONO	Locally Assigned
WORNAA	Unit Identification Code (UIC)	Ft. Sill, OK Garrison
S34031	Fiscal Station Number	DFAS-Lawton

Capabilities and Limitations. SOMARDS was designed as a budget execution system and accordingly is capable of capturing commitments, obligations and expenditures down to the document level. Based on the accounting classification data, SOMARDS summarizes data from individual transactions to reflect the status of funds (authorized, committed, obligated, disbursed and available) at various levels of detail (i.e., job order, suballocation, Army Management Structure Code, etc.) up to the budget line item and appropriation levels. SOMARDS is capable of capturing the cost of ND PP&E since it has PP&E general ledger accounts. However, the Army does not use these accounts to record ND PP&E. Instead, the disbursements (expenditures) are recorded as expenses.

SOMARDS was designed to capture depreciation, but it cannot calculate depreciation. SOMARDS uses codes to automatically post transactions to its general ledger accounts. However, it has an operational limitation since there are no codes to automatically post transactions to either the PP&E and depreciation general ledger accounts. Posting transactions to these accounts requires manual calculations and journal voucher entries.

Reporting. SOMARDS generates several reports. The primary report that the Program Management Office uses is the *Status of Approved Resources* (RCS CSCFA-218). This report shows funds authorized, committed, obligated, and disbursed by Army Management Structure Code. SOMARDS is the primary source of information for the budget execution 1002 Report.

Department of the Navy

In its FY 1999 financial statements the Navy reported in the narrative statement on yearly investments for ND PP&E, that:

Investment values included in this report are based on outlays (expenditures). Outlays are used instead of acquisition costs because current DoD systems are unable to capture and summarize procurement appropriation acquisition costs in accordance with accounting standards.

Procurement Appropriations fund the acquisition of Navy ND PP&E. For the Navy, there were seven Procurement Appropriations in the FY 2000 budget:

- Aircraft Procurement
- Weapons Procurement
- Shipbuilding and Conversion
- Other Procurement
- Procurement, Marine Corps
- Procurement of Ammunition
- National Defense Sealift Fund

Within these seven appropriations, there are individual budget line items, which are grouped by activity codes. For example, funds for the DDG-51 are appropriated in the Shipbuilding and Conversion appropriation. In the FY 2000 budget, there are 13 budget line items within this appropriation. The first five are in activity code 2 – Other Warships, the next two are in activity code 3 – Amphibious Ships, and the last six are in activity code 5 – Auxiliaries and Craft. In the FY 2000 budget, there is only one budget line item for the DDG-51 - number 212200 – under activity code 2. Unlike the Army and Air Force, the Navy has several commands that acquire ND PP&E.

Primary System The Navy uses the Standard Accounting and Reporting System (STARS) as its standard general fund accounting system. STARS, a mainframe computer database system, is used at both field and higher command levels and for departmental reporting purposes. It has an electronic invoice processing and payment capability. These capabilities are contained in four separate modules – Funds Distribution and Departmental Reporting (STARS-FDR), Headquarters Claimant (STARS-HCM), Field Level (STARS-FL), and One Pay Bill Paying (STARS-OP).

System Operation. The Defense Finance and Accounting Service – Cleveland operates STARS. Major commands, such as the NAVSEA, enter authorized funds received into STARS-HCM by budget line item. For Procurement Appropriations, funds can be suballocated to project levels within STARS-HCM, but further suballocations are not possible. Generally, organizations below the major command level, such as Program Executive and Program Management Offices, manage funds at a lower level of detail. For example, the DDG 51 Program Management Office uses a system that its higher command, the Program Executive Officer – Theater Surface Combatants, developed called the Financial Management Information System. This system is

capable of making further suballocations and is electronically linked with STARS through the Electronic Transfer of Funds System.

Transactions (commitments, obligations, and disbursements) are recorded in STARS using a document number that includes an accounting classification code. Typical document types include contracts, purchase orders, travel orders, project orders, work requests, military interdepartmental purchase requests, etc. STARS-HCM automatically interfaces with the other STARS modules, ten other finance and accounting systems, and two critical feeder systems. Like the Army, the Navy uses an accounting classification code for its transactions, the structure of which is presented in the Table D-6.

Table D-6

ACCOUNTING CLASSIFICATION CODE		
AA 17 5 1711 A224X 311 XQ WML 0 068342 2D 000000 21954 418 501 A		
Code	Data Element	Explanation
AA	Accounting Resource Number	
17	Department Code	Department of the Navy
5	Fiscal year (FY)	Fiscal Year 1995
1711	Appropriation Symbol	Shipbuilding and Conversion, Navy
A224	Subhead 1 st Position=Claimant 2 nd Position=Budget Activity 3 rd & 4 th Positions=P-1 Line	DDG-51 Guided Missile Destroyer
X	Reserved for future use	
311	Object Class	Property
XQ WML	Bureau Control Number 1 st & 2 nd Position=Participating Manager 3-5 Positions= Requiring Financial Manager	NAVSEA office (CO3K1) NAVSEA PMS 400 for Electronics
0	Suballotment	
068342	Authorized Accounting Activity	STARS – OPLOC Charleston
2D	Transaction Type	Normal Transaction Type
000000	Property Accountability Activity	Only used for RDT&E funds
21954	Project Unit	DDG 51 – Other Class Warships
418	Major Cost Category	NAVSEA Electronic Production COMP
501	Project Directive	AN/USQ-82V, DMS
A	Project Directive Line Item Suffix	

Capabilities and Limitations. STARS-HCM was designed as a budget execution system, and accordingly is capable of capturing commitments, obligations, and disbursements down to the document level. Based on the accounting classification data, STARS-HCM summarizes the data from individual transactions to reflect the status of funds (authorized, committed, obligated, disbursed, and available) at various levels of detail up to the budget line item and appropriation levels. STARS-HCM is capable of capturing the cost of ND PP&E since it has PP&E general

ledger accounts. However, the Navy does not use these accounts to record ND PP&E. Instead, the disbursements (expenditures) are recorded as expenses.

STARS-HCM was not designed to calculate or capture depreciation costs as it does not have a depreciation general ledger account.

Reporting. STARS-HCM is an interactive system and users have extensive capabilities to make on-line queries. As a result, the system does not produce periodic or recurring reports. Financial information from STARS-HCM is transmitted to STARS-FDR, which is the primary source of information for the budget execution 1002 Report.

Department of the Air Force

In its FY 1999 financial statements the Air Force reported in the narrative statement on yearly investments for ND PP&E that:

The yearly investment costs for aircraft, missiles and satellites along with associated support principal end items were extracted from the DOLARS-Status of Funds System, which prepares the ACCT-RPT(M)1002 report. To arrive at the costs reported, Budget Program Activity Codes (BPACs) were identified for each major category, by type (combat, airlift, other, ICBM, other missiles and satellites). Using these BPACs, an extract was then prepared to obtain the values reported. Excluded from our extract were BPACs reported for aircraft spares, repair parts, reimbursable program cost and undistributed costs. These costs were considered to be OM&S purchases.

Investment values included in the report are based on outlays (expenditures). Outlays are used instead of acquisition costs, because current DoD systems are unable to capture and summarize Procurement Appropriation acquisition costs in accordance with accounting standards.

Procurement Appropriations fund the acquisition of Air Force ND PP&E. For the Air Force, there were four Procurement Appropriations in the FY 2000 budget.

- Aircraft
- Missile
- Ammunition
- Other

Within these four appropriations, there are individual budget activity codes. For example, the Aircraft Procurement Appropriation contains seven budget activity codes.

- 1 – *Combat Aircraft*
- 2 – *Airlift Aircraft*
- 3 – *Trainer Aircraft*
- 4 – *Other Aircraft*
- 5 – *Modification of In-service Aircraft*

6 – Aircraft Spares and Repair Parts

7 – Aircraft Support Equipment and Facilities

Funds for the F-15 program are budgeted and appropriated in budget activity code 1 - Combat Aircraft. This activity code also contained funding for the F-22, Raptor, and the F-16C/D. The Spares and Repair Parts and Support Equipment and Facilities budget activity code also included funds for the F-15 program. Like the Army, there is one major command – Air Force Materiel Command - that acquires the majority of ND PP&E.

Primary System. The Air Force uses the General Accounting and Finance System (GAFS) as its general fund accounting system. It is used by all major commands, including Air Force Materiel Command and its centers.

System Operation. Defense Accounting and Finance Service – Denver operates GAFS, which is a mainframe computer database application. It accommodates standard appropriation accounting transactions including fund authority, commitments, obligations, disbursements, and balances of available funds. Upon receipt of fund authority, DFAS sets up the fund authority in GAFS by Budget Procurement Activity Code.²⁹ GAFS does not have the capability to make further sub-allocations.

Transactions (commitments, obligations, and disbursements) are recorded in GAFS using a document number that includes an accounting classification code. Typical document types include contracts, purchase orders, travel orders, project orders, work requests, military interdepartmental purchase requests, etc. GAFS has interfaces with at least 11 different systems such as accounts receivable, accounts payable, civilian payroll, and procurement. Like the Army and Navy the Air Force uses an accounting classification code for its transactions, the structure of which is described in Table D-7.

²⁹ GAFS Budget Procurement Activity Code equates to the Budget Activity Codes.

Table D-7

ACCOUNTING CLASSIFICATION CODE		
57 1 3010 111 47WL 830110 034110 14000 030117B 595600 F95600A		
Code	Data Element	Explanation
57	Department Code	Department of the Air Force
1	Fiscal year (FY)	Fiscal Year 2001
3010	Appropriation Symbol	Aircraft Procurement, Air Force
11	Fund Code	Aircraft Procurement
1	Fiscal year (FY)	Fiscal Year 2001
47	Operating Agency	Air Force Material Command
WL	Operating Budget Accounting Number	Wright Patterson Air Force Base
830110	Budget Procurement Activity Code/Major Force Program	Aircraft Procurement
034110	Cost Center/Material Program Code	F-15 program
14000	Element of Expense Expense/Investment Code	
03117B	Program Element	F-15 Aircraft
595600	Accounting & Disbursing Station Number	Wright Patterson Air Force Base Accounting Station
F95600	Customer Name	Department of Defense

GAFS uses a hierarchical indexing scheme for access to the database. This indexing scheme is built into the application software and the business processes. GAFS functions as a “net system” meaning that it reflects the current balance available based on funds authorized, committed, obligated, and disbursed.

Capabilities and Limitations. GAFS was designed as a budget execution system and accordingly it is capable of capturing commitments, obligations, and expenditures down to the document level. Based on the accounting classification data, GAFS summarizes the data from individual transactions to reflect the status of funds (authorized, committed, obligated, disbursed, and available) at various levels of detail up to the Budget Procurement Activity Code and appropriation levels. GAFS is capable of capturing the cost of ND PP&E.

GAFS was not designed to capture or calculate depreciation.

Reporting. Information on certain contractor payments is captured in the Central Procurement Accounting System (CPAS), which, in turn, provides data to both GAFS and the Command On-line Accounting and Reporting System (COARS). GAFS currently does not provide consolidated financial reports. Except for data that CPAS provides to both GAFS and COARS, data contained in GAFS is fed directly to COARS. In turn, COARS feeds information to the Department On-Line Accounting and Reporting System, which is the primary source for the budget execution 1002 Report. The Defense Finance and Accounting Service currently uses the Departmental On-Line Accounting and Reporting System for financial reporting.

Accounting System Summary

As discussed, the Army and the Navy systems do have PP&E general ledger accounts. However, the Navy does not use the PP&E general ledger accounts system to capture the cost of ND PP&E acquisition programs--not individual ND PP&E items--and the system does not have a depreciation general ledger account. The Army system requires manual computations to make entries to record data in the PP&E and depreciation general ledger accounts. The Army does not use these accounts to capture the cost of ND PP&E. The Air Force system does not have PP&E or depreciation general ledger accounts, thus it is not capable of capturing the costs of ND PP&E. The DoD plans to make improvements to the Navy and Air Force systems and replace the Army system. In its Financial Management Plan, dated September 1999, the DoD reported that:

- SOMARDS will be eliminated and replaced with the Defense Joint Accounting System.
- STARS is a primary general fund accounting system, but it is not fully compliant federal standards. However, STARS will be used to consolidate all DON general fund accounting, commercial entitlement and reporting operations.
- GAFS is being reengineered to (1) provide a relational database which operates in an open systems environment,³⁰ (2) be capable of integration with the DFAS Corporate database to update the general ledger using a the U.S. Standard General Ledger Chart of Accounts, and (3) incorporate acquisition accounting functionality and improve the processes associated with accounts receivable and payable.

Although the DoD is actively engaged in improving or replacing its accounting systems, completion of such changes will not be completed for many years and is frequently complicated by numerous factors. For example, we were advised that the Congress recently eliminated the funding for the Defense Joint Accounting System (DJAS), which was planned to replace SOMARDS. The DoD is presently working with the Congress to restore funding for the DJAS.

³⁰ *An open systems environment permits the applications to operate on any type of computer with any type of operating systems. This reduces the costs to operate and maintain a system.*

Appendix E – Components of Full Cost

Statement of Federal Financial Accounting Standard (SFFAS) Number 4 Managerial Cost Accounting Standards defines “full costs” as:

...the total amount of resources used to produce the output. This includes direct and indirect costs that contribute to the output, regardless of funding sources. It also includes costs of supporting services provided by other responsibility segments or entities.

The full cost of ND PP&E includes payments to contractors, program management costs, as well as other direct and indirect costs. Based on the foregoing definition and the three weapon systems selected for review, we identified those costs that could be included as part of full costs. Table E-1 provides a list of cost categories, the type of cost and a brief description.

Table E-1

<i>Category</i>	<i>Type</i>	<i>Description</i>
Costs paid to contractors (i.e., Procurement Costs)	Direct	This represents the costs paid directly to ND PP&E contractors.
Property and Equipment (including Special Tooling and Special Test Equipment) in the possession of, or acquired directly by, the Government and delivered or otherwise made available to a contractor for use in accomplishing a contract.	Direct	This represents costs associated with producing Major End Items or Other ND PP&E.
Program management office salaries (i.e., Military and Civilian Pay)	Direct	These costs are for the salaries of individuals that manage an ND PP&E acquisition program.
Program management office operations (i.e., office equipment, supplies, utilities, technical support)	Indirect	These costs represent expenses associated with managing a ND PP&E program.
Office of the Under Secretary of Defense for Acquisition, Technology & Logistics	Indirect	These are the costs of managing the overall DoD acquisition process.
Service Specific Oversight – Assistant Secretary of the Army for Acquisition, Logistics & Technology; Assistant Secretary of the Navy for Research, Development & Acquisition; and Assistant Secretary of the Air Force for Acquisition	Indirect	These are the costs associated with the oversight of the acquisition process by the Military Departments.
Defense Contract Management Agency	Indirect	These costs relate to the management of contracts. DCMA's FY 2000 budget is less than 1.5 percent of the DoD's ND PP&E acquisition budget.
Defense Finance and Accounting Service	Indirect	These costs relate to transaction processing and general accounting. DFAS's FY 2000 budget is less than 2.3 percent of the DoD's ND PP&E acquisition budget and DFAS costs associated with supporting ND PP&E acquisition is less than 0.2 percent of the DoD's ND PP&E acquisition budget.
Defense Contract Audit Agency	Indirect	The costs relate to audits of acquisition program contracts. DCAA's FY 2000 budget is less than 0.5 percent of the DoD's ND PP&E acquisition budget.

Based on our limited evaluation of the indirect costs identified above, KPMG concluded that these costs are not likely to be material to ND PP&E reported on the financial statements or to

individual acquisition program disclosures. The following paragraphs more fully describe certain components of the information in Table E-1.

Program Management Office

KPMG obtained the estimated costs to operate the offices of the program management offices for the Abrams Tank Systems and DDG-51 acquisition programs.

The Program Manager, Abrams Tank Systems advised KPMG that it has a staff of 7 military and 29 civilian personnel with additional staffing provided on a part time basis. Projected FY 2000 costs are estimated at \$11.4 million. This cost is funded from the RDT&E and Procurement appropriations (except for military personnel costs which are funded by the Military Personnel appropriation).

The program manager for the DDG-51 advised KPMG that it has a staff of 5 military and 26 civilian personnel. Projected FY 2000 costs are estimated at \$2.6 million. This cost is funded by the Operations and Maintenance appropriation (except for military personnel costs which are funded by the Military Personnel appropriation).

Indirect Costs

KPMG identified four types of indirect costs associated with the acquisition of ND PP&E.

Oversight

The Office of the Under Secretary of Defense for Acquisition, Technology & Logistics provides oversight to the three Military Departments in addition to being responsible for oversight of the technology and logistical functions. Within the Military Departments, Assistant Secretaries provide oversight to the various Program Executive Offices in addition to being responsible for other functions. In turn, the Program Executive Offices provide oversight to multiple program management offices. Although KPMG was not able to obtain the costs associated with these oversight functions, we question whether such broad-based oversight functions should be allocated to ND PP&E acquisition programs.

Defense Contract Management Agency (DCMA)

The DCMA is responsible for a wide variety of contract management functions to include (1) establishing overhead rates, (2) reviewing and approving progress payments, (3) clarifying contracts, (4) reviewing the status of contractor processes, (5) accepting products (6) monitoring Government property, (7) privatizing depots, (8) closeout and (9) contingency contract closeout. These services apply to numerous types of contracts and functions, many of which are not associated with the acquisition of ND PP&E. The DCMA's total FY 2000 budget totals about \$1.1 billion, less than 1.5 percent of the DoD's ND PP&E acquisition budget.

Defense Finance and Accounting Service (DFAS)

The DFAS consists of five centers and 19 operating locations with about 20,000 employees and a FY 2000 budget of \$1.7 billion. The DFAS performs a wide variety of finance and accounting

services to include payroll operations for civilian, military and retired military personnel, debt management, payments for travel and transportation along with payments to contractors. For FY 2000, DFAS estimated that \$138.8 million of its budget related to making payments to contractors. This cost relates to all contractor payments – not just ND PP&E contractor payments. This amount is less than 0.5 percent of the DoD's ND PP&E acquisition budget.

Defense Contract Audit Agency (DCAA)

The DCAA consists of some 300 offices with about 4,000 employees. The DCAA is responsible for providing standardized contract audit services for the DoD, as well as accounting and financial advisory services regarding contracts and subcontracts for all DoD Components that are responsible for procurement and contract administration. The DCAA provides these services in connection with negotiation, administration, and settlement of contracts and subcontracts. The DCAA also provides contract audit services to other government agencies. The DCAA's FY 2000 budget, which funds services for many types of contracts – not just those associated with ND PP&E - is \$360 million, less than 0.5 percent of the DoD's ND PP&E acquisition budget.

Summary

The DoD's FY 2000 budget contained a request for \$34.4 and \$53.0 billion respectively for the Research, Development, Test and Evaluation and Procurement appropriations for a total of \$87.4 billion. Of this amount, non-ND PP&E acquisition program budgets total in the range of \$6.4³¹ to \$12.4 billion. Using this FY 2000 budget information, we estimate that budgeted acquisition cost of ND PP&E programs could range from as little as \$75.0 billion up to as much as \$81.0 billion.

On a macro-level, the indirect costs related to DCMA, DFAS and DCAA activities total at most \$1.6 billion.³² These costs are associated with the management of thousands of contracts, many of which are unrelated to ND PP&E acquisition programs. Using the lower range of \$75.0 billion as the cost of ND PP&E, these indirect costs would add, at most, an additional two percent to the cost of individual ND PP&E acquisition programs.

³¹ KPMG calculated the \$6.4 billion as follows – DoD's Procurement appropriations contain amounts for acquisition of non-ND PP&E such as ammunition (\$2.0 billion), chemical demilitarization (\$1.2 billion), and Defense-wide procurement (\$2.1 billion) Also, DoD's RDT&E appropriations contain \$1.1 billion for basic research, which is generally not readily identifiable to specific ND PP&E.

³² This is comprised of DCMA's and DCAA's FY 2000 budgets of \$1.1 billion and \$360 million, respectively and DFAS's estimate of \$138.8 million relating to payments to contractors.

Appendix F - Acronyms

ACAT – Acquisition Category
AFEMS – Air Force Equipment Management System
AIRRS – Aircraft Inventory and Readiness Reporting System
AMSCO – Army Management Structure Code
CAIMS – Conventional Ammunition Inventory Management System
CBSS – Craft and Boat Support System
CBS-X – Continuing Balance System-Expanded
CEMS – Comprehensive Engine Management System
CFO – Chief Financial Officer
DAES – Defense Acquisition Executive Summary
EIMSURS – Equipment Inventory, Multiple Status, Utilization Reporting Subsystem
FASAB – Federal Accounting Standards Advisory Board
FASB – Financial Accounting Standards Board
FYDP – Future Years Defense Program
GAFS – General Accounting and Financial System
GASB – Governmental Accounting Standards Board
GCSAS – Generic Configuration Status Accounting Subsystem
LOGSA – Logistical Support Agency
MILCON – Military Construction
MILPERS – Military Personnel
NAVSEA – Naval Sea Systems Command
ND PP&E – National Defense Property, Plant, and Equipment
NVR – Naval Vessel Registry
O&M – Operations and Maintenance
PPBS – Planning, Programming, and Budgeting System
PP&E – Property, Plant, and Equipment
PPS – Product Performance Subsystem
RDT&E – Research, Development, Test and Evaluation
REMIS – Reliability and Maintainability System
RSSI – Required Supplementary Stewardship Information
SAR – Selected Acquisition Report
SFFAC – Statement of Federal Financial Accounting Concept
SFFAS – Statement of Federal Financial Accounting Standard
SOMARDS – Standard Operations Maintenance Army Research and Development System
SPBS-R – Standard Property Book System-Redesigned
STARS – Standard Accounting and Reporting System